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The Economic Situation in the Community

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Contents

	Page
I. The overall situation	3
A. *Balance sheet for 1970 and problems of short-term economic policy at the beginning of 1971*	7
1. The world economic situation in 1970	10
2. Demand	12
3. Production and employment	15
4. Balance of the markets	17
B. *Forecasts for 1971*	25
II. The situation in each of the Community countries	33
A. *Germany*	35
1. Balance sheet for 1970	35
2. Outlook for 1971	42
B. *France*	49
1. Balance sheet for 1970	49
2. Outlook for 1971	57
C. *Italy*	67
1. Balance sheet for 1970	67
2. Outlook for 1971	74
D. *The Netherlands*	83
1. Balance sheet for 1970	83
2. Outlook for 1971	89
E. *Belgo-Luxembourg Economic Union*	97
Belgium	97
1. Balance sheet for 1970	97
2. Outlook for 1971	103
Luxembourg	111
1. Balance sheet for 1970	111
2. Outlook for 1971	115
Annex: Commission Memorandum to the Council on the economic situation in the Community	121

Note :
This survey was completed around mid-November 1970. As regard the most recent developments and where it has not been possible to take them into account because of the pace at which national statistics are prepared and the time it takes to publish the survey in five languages, the latest issue of the "Graphs and Notes on the Economic Situation in the Community" can usefully complete the information supplied here.

I. THE OVERALL SITUATION

The vigorous economic expansion recorded in the Community since the middle of 1967 continued in 1970. However, production advanced less than in previous years. From 1969 to 1970, real gross Community product rose by 6 %, compared with 7 % from 1968 to 1969 and 6 % from 1967 to 1968. Since 1957, it has increased by 95 %, compared with 61 % in the United States and 42 % in the United Kingdom. The gross Community product in money terms expanded by 12 ½ % from 1969 to 1970, repeating the performance of the year before; it is now slightly less than $500 000 million, compared with $970 000 million for the United States and $116 000 million for the United Kingdom.

Overall demand in terms of money continued to expand rapidly in 1970. The Community's visible exports to non-member countries rose more vigorously than in 1969, despite the weak economic trend in the United States and the United Kingdom.

Internal demand expanded at much the same rate as in 1969. Stockbuilding had a delaying effect on the upward trend while gross fixed asset formation, in terms of value up by some 18 ½ % as against 15.5 % in the previous year, provided very vigorous stimuli.

Expenditure on consumption expanded slightly faster still than in 1969, mainly owing to the sharp wage increases. Wage incomes rose by 10 to 20 %, according to the member country concerned. In contrast, the rise in income from entrepreneurship and property was weaker than from 1968 to 1969, entailing an appreciable shift in the distribution of incomes in favour of wage and salary earners.

Production failed to keep up with the expansion of demand. Agricultural production contributed little if anything to the increase in internal supply. Industrial production, on the other hand, rose by 8 %, but its growth slowed down distinctly, both in comparison with the previous year as a whole (11%) and in terms of the trend during the year.

The growth in real value added was insufficient, measured against the rise in overall demand in money terms; this was mainly because reserves of technical capacities and manpower were almost exhausted. In some industry groups, particularly some basic materials and consumer goods industries, however, stockbuilding by dealers and manufacturers also acted as a brake on the expansion of production.

In certain member countries, the number of unemployed in the summer was down to a level that could hardly be reduced any further. In the second half of the year, however, there were already signs here and there of a tendency for the situation on the labour markets to ease.

Owing to the wide discrepancy between internal supply and overall demand, the growth in the Community's imports from non-member countries remained very dynamic. The Community thus made a major contribution to world economic activity.

Although internal production was supplemented by imports, prices in the Community showed an unusually sharp rise. In no single year since the entry into force of the Treaty of Rome have they climbed as rapidly as from 1969 to 1970.

Even though all Member States pursued a policy of monetary and credit restraint during the greater part of the year, the rise in the volume of credit was hardly weaker than in 1969. Surpluses from transactions with abroad, in addition, substantially augmented internal liquidity. The Community's current account deteriorated distinctly, but the capital account showed heavy surpluses, in contrast to developments last year. During the first ten months official gross gold and foreign exchange reserves in the Community rose by some $6 800 million, whereas in 1969 as a whole they had fallen by $1 700 million.

The slowdown in economic growth which started in 1970 will probably continue in 1971.

The expansion of overall demand in money terms is likely to slacken distinctly. Current expectations are that the Community's visible exports will grow by 8 %, following a rise of 14 % in 1970. Among the components of internal demand, gross fixed asset formation in particular will expand more sluggishly. As order books are still well filled, actual investment spending can still be expected to rise appreciably in the early months of 1971. Subsequently, however, the calmer tendency already to be seen in entrepreneurs' propensity to invest may gain ground more and more. All in all, expenditure on gross fixed asset formation is likely to go up by 10 ½ %, as against 18 ½ % in 1970.

The rise in private consumers' expenditure will not slow down quite as sharply, being expected to fall from 12% to 10%. The expansion of mass incomes is likely to remain strong and lose momentum only gradually.

At first the supply of goods will not keep up with the still comparatively vigorous expansion of overall demand. The Commission's departments expect that from 1970 to 1971 the real gross Community product will grow by 4 ½ %, taking into account the prospective increase in capacity and the available manpower and assuming that in some industries the currently still extremely high degree of capacity utilization will fall in the course of the year.

This outlook implies that full employment will be maintained. At the same time, there is a great risk of prices rising further; the upward thrust of wage costs will play a major part here. Economic policy in 1971 will therefore be faced with the difficult task of stabilizing prices and costs while preventing a cumulative slow-down in economic growth.

A. Balance sheet for 1970 and problems of short-term economic policy at the beginning of 1971

The year 1970 saw the continuation of boom conditions in the Community. Incomes and demand went on expanding at a very rapid pace. Towards the end of the year, the gross Community product was almost $500 000 million, as against $ 175 000 million when the Treaty of Rome came into force. Although in many sectors the growth of production was impeded by an acute labour shortage and a shortage of technical capacities, the rise from 1969 to 1970 was still very appreciable: gross Community product in real terms expanded by 6 %. Employment continued to rise in all member countries. Owing to the strong pull of demand, the strains, very heavy in 1969 already, mounted further during much of the year, so that the rise in costs and prices gathered momentum. In contrast to developments between 1965 and 1969, the pace of price increases in the Community no longer showed great differences from one country to another. Together with the parity changes in 1969, this contributed to a more even development of the trade balances and the overall balances of payment in the Community.

It should, however, be noted that the "harmonization" of the rates of price increase occurred at too high a level and that in some member countries it was, compared with 1969, accompanied by a very appreciable acceleration in the pace of increase.

Visible trade with non-member countries had only a comparatively small inflationary influence on the Community. It is true that the increase in costs and prices generally recorded throughout the world had quite noticeable effects within the Community, not least because without it the balance of payments trend in the Community would have been considerably more unfavourable and have substantially increased the pressure to stabilize the internal cost trend. But in 1970 the non-member countries called on the Community's resources in appreciably smaller measure than in preceding years. The Community's balance of trade, which in 1968 showed a surplus of $ 1 700 million and was in equilibrium in 1969, closed in 1970 with a deficit of some $1 400 million. The surplus on current account fell at the same time.

The rise in world market prices for industrial raw materials, which in 1969 was a major factor forcing up prices, has given way to a distinct decline since the spring of 1970.

A look at the liquidity flows, however, reveals a different situation. While as recently as last year foreign exchange transactions with abroad tended to reduce domestic liquidity, in 1970 the Community has recorded a substantial net inflow of liquidity from non-member countries.

This reversal in trend is largely the result of the conflicting lines of monetary and credit policy pursued on the one hand in the United States, where restrictions were gradually relaxed in the course of the year, and on the other hand in the Community countries, where the restrictive course was maintained. In spite of several, albeit limited, adjustments of interest rates and especially of discount rates, the inflow of short-term capital into the Community remained considerable throughout 1970.

While the figures for 1970 as a whole clearly bear the mark of the boom, an analysis of developments during the year reveals that in most member countries the economic trend has shown signs of entering a less overheated phase.

Pointers in this direction include the decline in new orders, the slowdown of activity in several basic materials industries, especially steel, and the weak trend of demand in some traditional consumer goods industries, where dealers have pursued a cautious stockbuilding policy. The flow of orders for plant and machinery has also lost in vigour in some member countries.

As, at the same time, a large number of industries have still been faced with bottlenecks in production, the combination of these factors has led to an appreciable slowdown in the expansionary trend of industrial production in the past few months.

This has a yet had little if any effect on the labour market. In the countries where manpower was particularly difficult to find at the beginning of 1970, the shortage remains acute.

Nor has the less dynamic trend in new orders for industry so far been reflected in the movement of prices; this movement is still distinctly upwards, apart from a temporary and seasonal slowdown in the summer. The factors making for the upward thrust of prices have, however, changed in character: until the middle of 1970 the key factor had been the imbalance between supply and demand, but since then the sharp rise in costs has been increasing in importance.

In the Community as a whole, the main points to be considered in laying down the primary aims of economic policy at the turn of the year are the growth of production and demand, maintenance of the full employment trend, the continued surplus on current account and the persistence of a rapid rise in prices.

From this and the outlook for the economic trend set out in Part C of this Chapter it clearly follows that the main problem for short-term economic policy in the months ahead lies in reducing the rise in prices to satisfactory proportions without touching off a cumulative slowdown in economic expansion.

Indeed, while the other indicators are moving roughly in conformity with the target figures shown in the draft of the third Medium-term Economic Policy Programme, current rates of price increase and those expected for the months ahead are substantially above the target figures which the Programme shows for the period 1970-75.

In 1970, all Member States distinctly tightened the restrictive line of their short-term economic policy. During the year the stress was increasingly on fiscal measures. This was in conformity with the guidelines laid down in the Commission memoranda of 22 December 1969[1] and 7 July 1970[2] on the Community's economic policy; the conclusions of both documents had been endorsed by the Council.

The current and prospective tendency for prices to rise, and the reasons for this tendency, undoubtedly stem in considerable measure from the fact that in recent years the struggle against inflation has not always been conducted with sufficient speed and energy. Transactors have therefore developed patterns of inflationary behaviour which may persist for a while even in the event of a distinct easing in the supply-demand relationship.

In this context it is significant to note that the abatement in the expansion of demand observed in the past few months has not been accompanied by any appreciable slowing of the rise in wages. On the contrary, in some countries the rise has of late tended to gather momentum. The upward thrust of prices thus engendered is all the stronger as the advance of productivity in the economy has slowed down considerably, the result being that the rise in wage costs per unit of output is unusually rapid in the Community at the moment.

Entrepreneurs are trying to counteract the resultant pressure on profit margins by adjusting their prices; despite the slower expansion of demand, they can do this successfully where competition is not effective enough. Since in most member countries there are statutory arrangements or agreements between the two sides of industry under which wages are raised more or less automatically when consumer prices go up, this keeps the wage-price spiral in motion.

Consequently, there is still a need for a policy of economic consolidation designed to stabilize costs and prices. Such a policy will produce the desired results only if it is pursued by all Member States simultaneously. In doing so, governments may closely concert their action, taking due account of the differing situations in the various member countries, especially as regards the level of demand, the situation on the labour market, and the foreign trade and payments position.

Since the causes of the inflationary tendencies have increasingly shifted from the expansion of demand to the trend in costs, the measures that have a restrictive influence on overall demand should not be tightened further at the moment. Nor should there be an unduly early relaxation in the restrictive course that is being pursued. In this context there appears to be a case for

[1] «Memorandum from the Commission to the Council on the Community's economic policy in 1970», 22 December 1969, given in Quarterly Survey No. 1/1970 on «The Economic Situation in the Community».

[2] «Memorandum from the Commission to the Council on the economic situation in the Community», 7 July 1970, given in Annex I to this Quarterly Survey.

changing the mix of the various ingredients of economic policy. This is particularly true of monetary and credit policy, where, in line with the downward trend of interest rates on the major international capital markets, a further downward adjustment of interest rates may well be called for in some countries, particularly Germany, the Netherlands, Belgium and France, to stem the inflow of liquidity from abroad. The instruments of liquidity policy, on the other hand, should continue to be applied along restrictive lines. The introduction of a minimum reserve on increases in bank liabilities in Germany, and the proposed computation of minimum reserves on the basis of bank lending in France, constitute in this context interesting experiments which may help to exert greater pressure on the liquidity of the economy in general.

Given the limits which the foreign trade and payments situation sets to credit policy, the part which the public finances play in management of the economic trend must be all the greater. In almost all member countries the restrictive effects of the 1970 budgets were smaller than originally intended. The draft budgets for 1971 generally point to a vigorous rise in public expenditure, which in some member countries largely exceeds the growth of the gross national product in terms of money that can be expected even after a vigorous rise in prices has been taken into account.

Another question is whether, later in the year, it will not be possible to consider an expansionary budget policy, especially when it is borne in mind that there is leeway to make up in important investments in infrastructure. But this presupposes a further calming down in the expansion of demand and a distinct tendency for costs and prices to stabilize. In the early months of the year the budget should in any case be handled in a way which will maintain its restrictive effect on overall demand, particularly since the public authorities provide important pointers for the behaviour of the other transactors. This implies that public contracts will have to be placed somewhat later than originally planned and that certain types of expenditure will have to be blocked for a time or paid into a contingency reserve.

In present circumstances an active employment policy is exceptionally important in all member countries. The prospective slowdown in the growth of production in some branches will not necessarily lead to substantial easing of the situation on the labour market, especially since any workers who become available will, because they live too far away or do not have the right skills, be far from meeting the requirements of other industries. So the chances are that the dynamic sectors of the economy will continue to suffer from labour shortages unless measures are taken to promote occupational and geographical mobility. From the angle of the economy as a whole, one of the major reasons why this situation gives rise to concern is that in most cases the dynamic industries are wage leaders, setting the pattern for the wage trend in less expansionary sectors; hence, in the economy as a whole there may be unduly sharp wage increases that are incompatible with the need to maintain steady economic growth. An active employment policy should, moreover, cover workers against the risk of temporary reductions or losses of income.

In present conditions, the greatest importance attaches to concerted action by both sides of industry and the authorities responsible for economic policy. The aim should be to bring the trend in money incomes into line with the need to restore internal equilibrium. This is the only way, without prejudicing full employment, of putting an end to a situation where the rise in costs and the rise in prices feed on each other. The current late phase of the boom is hardly a good occasion for changing the distribution of income through wage disputes, since this would be at the expense of investment activity and consequently of the level of employment or at the expense of the real purchasing power of workers. The future trend in incomes —both from profits and from paid employment—should instead be guided more strongly by the medium-term advance in productivity.

This should help to ensure an adequate rise in the various types of income while making it possible to stabilize the level of prices and bring about an appropriate increase in investment activity. For enterprises this means taking advantage of the quantity boom while exercising restraint in their price policy, an approach that could also be promoted by moves to intensify competition.

1. The world economic situation in 1970

World economic activity in 1970 remained on the whole very dynamic. Contrary to general expectations at the end of 1969, trade again expanded with great vigour, with the continued boom in the Community and the consequent steep rise in imports providing the main stimuli. Furthermore, in many industrialized countries, particularly the continental EFTA countries and Japan, there was little if any easing in the pressure of domestic demand despite the restrictive measures taken by governments; as a result, imports into these countries expanded vigorously. Even in the United States the stagnation of real gross national product from 1969 tot 1970 did not prevent the growth rate of imports from being almost as high as in 1969, since the propensity to import, especially in the first half of the year, was substantially stronger than in earlier periods of economic stagnation. In the United Kingdom, imports rose even more vigorously than in 1969, although the pace of economic expansion was weak. Lastly, imports by developing countries also climbed strongly, and trade with the state-trading countries showed a distinct upward tendency.

For the full year, the value of world imports, including EEC member countries' imports from each other and from non-member countries but excluding imports by the state-trading countries, will probably have risen by 13 %, compared with 13.5 % in 1969. However, given the sharp price increases, which averaged some 5 % over the year, expansion in real terms was considerably weaker.

In the *United States,* the economic trend was marked during much of the year by a decline in industrial production, while the upward thrust of prices and costs abated only slowly. In business circles, the propensity to invest weakened distinctly as the year advanced. In the autumn, new orders for plant and equipment were therefore at a considerably lower level than a year earlier. Stockbuilding also contributed to the slackening in economic activity. In addition, Federal expenditure, especially on defence and on space projects, showed a clear downward tendency. Unemployment rose vigorously. The unemployment rate (proportion of unemployed in the labour force) was about 5 ½ % in the autumn.

In the second half of the year, however, most economic indicators pointed to an improvement in the situation—apart from the direct and indirect repercussions of the strikes in the motor industry. Since the middle of the year there has, for instance, been a revival in residential construction and in the trend of production in the industries associated with it. Thanks to the appreciable rise in the disposable incomes of households and despite a sharp increase in the savings ratio, private consumption expanded somewhat more vigorously again, even though in real terms the advance was still fairly sluggish. Business activity may also have been boosted significantly by the more expansionary line of monetary policy since the spring, reflected in November in a reduction of the discount rate from 6 % to 5.75 %, and by the Federal budget, which has been in considerably heavier deficit since the second quarter.

Real gross national product, which after seasonal adjustment had in the first quarter been 0.8 % down on the previous quarter, increased in the second quarter by 0.15 % and in the third quarter by 0.4 %. In the fourth quarter, however, the upward trend will probably have been interrupted because of the persistent strike in the motor industry. When the average for the year is taken, real GNP will probably be slightly down on 1969, after a rise of 2.8 % from 1968 to 1969.

For the full year, the expansion of imports in terms of value was, at 9 %, about as vigorous as in 1969, despite the slowdown recorded in the second half of the year, since in the first half their level had been unusually high in relation to the weak economic trend. However, as the expansion of exports remained very lively until the end of the year, the trade surplus was substantially higher than a year earlier. For 1970, it probably ran at some \$3 000 million, as against \$640 million in 1969. Although this brought an appreciable improvement on current account, the overall balance of payments again closed with a very heavy deficit.

In the *United Kingdom,* the main features of economic developments in 1970 were a weak trend in production, rising unemployment and a faster upward movement of prices and costs.

A comparison with 1969 figures shows that for all components of domestic demand expansion was negligible, with the trend in private consumers' expenditure falling distinctly short of what had been expected at the beginning of the year, although wages went up vigorously. The ensuing rise in personal incomes was appreciable, but was partly offset by the tax burden (progressive income tax); in addition, the savings ratio went up considerably, at least in the first half of the year. But the main factor impeding the real growth of private consumption was the steep rise in prices; in 1970, consumer prices rose by some 8 % on the previous year. Gross fixed asset formation declined slightly in the first half of the year; in the second half this trend will probably have been reversed but, mainly because of the growing pressure of costs, the recovery will no doubt have been modest. The contribution made to economic activity by stockbuilding was distinctly smaller than in the year before.

Although the world economic trend was favourable, the growth rate of exports in terms of value was, at some 9 %, considerably lower than in 1969; here the large number of stoppages throughout the economy and the dock strikes were probably major factors.

All in all, the real growth in the gross national product from 1969 to 1970 was probably about 1 %.

The comparatively strong propensity to import in the first half of the year slackened somewhat in the second half, primarily because the decision to abolish the import deposit scheme at the end of 1970 caused imports to be delayed. For the full year, the growth of imports in terms of value was higher than last year (9 % as against 5 %), despite the very weak growth of economic activity at home; the balance of trade therefore deteriorated appreciably. The current account nevertheless still showed comparatively heavy surpluses, which enabled the United Kingdom to repay part of its foreign debts.

In the *other industrial countries,* expansion continued at a rapid pace in 1970. In some of them, especially the Scandinavian countries, it was accompanied by mounting inflationary strains engendered by the faster growth in domestic demand. In an effort to combat these strains, the governments of a number of countries gradually tightened the restrictive measures they had been taking since 1969. These measures were, however, very slow in producing effects; only in the closing months of the year was there evidence in some of the countries concerned that the expansion of demand was slowing down. All in all, the rise in the value of imports by industrialized non-member countries was appreciably stronger than last year, despite some slackening in the second half of the year. Imports by the EFTA countries in particular rose very rapidly; in terms of value they were 14 % up on 1969.

Switzerland enjoyed a distinct boom in 1970. At the end of the year, economic expansion was still lively, notably because of dynamic export demand and the stimuli which it provided. Even though growth has slowed down a little in recent months, the real growth in gross national product is unlikely to be smaller than in 1969 (5 %). As in the previous year, imports again rose particularly fast, their value advancing by 22 %. The surplus on current account fell sharply.

In *Sweden,* economic growth in 1970 was smaller than in 1969 but still remained fairly considerable; real gross national product expanded by some 4 ½ % as against 5.8 % in 1969. Little progress was made towards better internal and external equilibrium, a circumstance which forced the Government to tighten its restrictive policy. The pressure on costs and prices mounted even further during the year, and the Government twice ordered a price freeze: at the end of August for food, and in October for the remaining goods and services. With imports in 1970 some 20 % up on 1969, the foreign trade deficit increased considerably. As the balance of service transactions was also in deficit, the current account deteriorated further in 1970.

In *Denmark,* the tendency towards internal and external disequilibrium that had emerged in 1969 continued in 1970, even though monetary and budgetary restrictions were tightened increasingly. The expansion of domestic demand remained lively. The rise in prices and costs gathered momentum, and in October the authorities ordered a temporary price freeze. Imports advanced rapidly until the middle of the year and have since tended to decline. The balance of trade continued to deteriorate and the deficit on current account was much heavier than in 1969.

Norway also enjoyed a distinct boom in 1970. The rapid advance in domestic demand led to increasing recourse to imports, which in terms of value went up by more than 20 %. With exports expanding at a comparatively slow pace only, there was a distinct deterioration in the balance of trade and—largely as a consequence—in the current account as well.

In *Austria,* expansion continued rapidly in 1970, the trend in the first half of the year being comparatively stable. Investments by industry, which had stagnated for several years, picked up appreciably; private consumers' expenditure has tended to gather momentum in recent months, and export demand has continued to be very dynamic. Owing to the lively growth in overall demand, the propensity to import was particularly vigorous and the value of the country's purchases abroad was some 25 % up on the figure for the previous year. Consequently, the balance of trade deteriorated appreciably, and the surplus on current account was considerably smaller.

In *Spain,* the economic trend in 1970 was no longer as favourable as in 1969. The growth of domestic supply was impeded by numerous strikes and by the effects on industry of the monetary and budgetary measures taken at the end of 1969, while the fall in the purchasing power of households, caused by sharp price increases and the wage freeze, considerably impaired the real expansion of private consumers' expenditure. Despite the introduction of an import deposit of 20 % at the end of 1969, imports still rose rapidly in the first half of the year and did not slow down appreciably till later in the year. The deficit on the balance of trade was therefore very heavy. The overall balance of payments may nevertheless have improved, owing to the vigorous rise in receipts from tourism, transfer incomes and a considerable inflow of capital.

In *Japan,* 1970 was again a year of rapid economic growth. Export demand continued to be very dynamic, and domestic demand was forcefully boosted by the rise in fixed investment and the expansion of private consumers' expenditure. Although in the closing months of the year there were signs of a slowdown in production in some industries, notably as a result of the credit restrictions and bottlenecks in capacity, the real gross national product rose by some 11 ½ % in 1970. The strains in the production apparatus were reflected in a rapid expansion of imports. As exports also went up vigorously, the balance of trade even improved slightly, compared with 1969. All in all, therefore, the lively growth of the Japanese economy in 1970 was such that the strong external position of this country, with its large surpluses on current account, was fully maintained.

In *Canada,* the economic trend in the first half of the year was somewhat more dynamic than in the United States. In the course of the year, however, economic activity tended to slow down under the impact of the economic situation in the United States and of the rise in value of the Canadian dollar since its rate of exchange was allowed to float on the foreign exchange markets. All in all, the real growth in the gross national product for 1970 will probably not exceed 2 %. Imports stagnated during the year, and their level for the full year was probably only slightly up on 1969. The balance of trade therefore improved distinctly in 1970, even though exports expanded only very slowly. The current account, which showed an appreciable deficit in 1969, was back in significant surplus in 1970.

In the first half of the year, exports by the *developing countries* were still stimulated by vigorous demand from the industrialized countries. At the same time, the considerable increase in the imports of the developing countries continued, notably because of the rise in their foreign exchange reserves. The second half of the year brought a certain slowdown in both exports and imports. Nevertheless, for the full year the growth in imports in terms of value was again slightly higher than the year before. All in all, the trade balances of the developing countries tended to deteriorate in the course of 1970 because the trend in the export proceeds of these countries was less favourable, influenced as it was by the appreciable fall in world market prices since the second quarter.

2. Demand

Overall demand in the Community continued to expand with great vigour in 1970, with the main stimuli coming increasingly from internal demand. In the second half of the year, however, the rise in demand tended to calm down distinctly.

Owing to the buoyancy of the world business situation, the Community's *exports* to non-member countries also expanded very rapidly on the whole, despite a certain tendency to slow down in the second half of the year. For the full year, the increase in terms of value was 14 %, compared with 11 % in 1969. Given the sharp rise in prices of export goods, however, the increase in real terms was, at some 9 %, appreciably less lively.

The Community's exports to industrialized countries expanded very briskly in 1970. While the Community countries benefited comparatively little from the strong propensity to import observed in the United States in the past two years and deliveries to United Kingdom were also slow to rise, the sustained boom in most EFTA countries accelerated Community sales to these countries very vigorously. The value of exports to Switzerland, Sweden, Austria and Portugal, for instance, was more than 20 % up on the figures for the previous year. There was at the same time a vigorous rise in exports to other important trading partners of the Community, especially Spain, Yugoslavia, Japan and South Africa. In addition, exports to the developing countries rose throughout the year more briskly than in 1969; deliveries to the associated overseas countries in particular expanded very rapidly. The rise in sales to the state-trading countries again gathered momentum.

Internal demand in the Community grew very vigorously in 1970; there was not only a strong rise in what a year ago had already been a very high level of investment activity, but the rise in consumption also gained in strength.

Gross fixed asset formation in terms of value rose by some 18 ½ % from 1969 to 1970, compared with 15 ½ % from 1968 to 1969. In terms of volume, however, the advance was smaller than a year earlier (some 8 % as against 9.2% in 1969), owing to the considerably faster rise in prices.

The most dynamic component was *investment by enterprises in plant and machinery,* which showed an unusually vigorous rise. In the second half of the year, the marked investment boom in trade and industry showed signs of calming down gradually, at any rate if one may judge by the trend of orders in the capital goods industries. After the unusually rapid expansion of investment activity in the past three years, this is a perfectly normal development; in part, however, it already reflects the heavy pressure which rapidly mounting wage costs are exerting on profit margins, as well as difficulties in finding funds from outside sources owing to the credit restrictions and, in some industries, to a less favourable sales outlook.

The expansion of *expenditure on building and construction* also remained unusually vigorous, but as prices in this sector were rising very sharply the advance in terms of volume was very limited. As in 1969, it was in industrial building that the rise was strongest in most member countries. Public expenditure on building and construction, too, generally expanded at a lively pace everywhere except in France, although the advance was nothing like as vigorous as that in capital spending by enterprises. Residential construction, on the other hand, grew only modestly in most member countries. The number of dwellings finished in the Community in 1970 was probably smaller than in 1969. The rapid rise in costs, the difficulty experienced in obtaining mortgage, and the high long-term interest rates severely hampered commencement of new residential construction work. Especially in Italy, the expansion of investment in residental construction weakened appreciably. In Germany and the Netherlands, the labour shortage was an additional factor hindering investment in residental construction. In Belgium, residental construction expanded less vigorously than in 1969, when work on residential buildings was stepped up sharply because of the tax reform (VAT) which was expected to enter into force on 1 January 1970. In France, fewer dwellings were completed in the first half of 1970 than in the corresponding period of the previous year. In the second half of the year, however, there was evidence of a slight revival in actual building starts after the residential building premiums blocked for reasons connected with the business situation had been unfrozen.

Stockbuilding generally made a less lively contribution to the expansion of economic activity than in 1969. In some industries, especially basic materials, textiles and footwear, the high cost of credit and shorter delivery periods prompted buyers to exercise great restraint in their stockbuilding policy during 1970. The fall in world market prices for industrial basic

Visible exports to non-member countries

(Values and % changes on preceding year)

	1969		1970			
	million u.a. [1]	Full year	1st quarter	2nd quarter	3rd quarter [5]	Full year [5]
All non-member countries	39 236	+ 11	+ 16.5	+ 15	+ 14	+ 14
of which :						
Industrialized countries [2]	25 605	+ 12	+ 20	+ 15	+ 15	+ 14
including :						
United States	5 958	+ 3.5	+ 22.5	— 1.5	+ 9	+ 9
EFTA	12 744	+ 13.5	+ 18.5	+ 21	+ 15	+ 18
United Kingdom	3 364	+ 7.5	+ 4.5	+ 9.5	+ 0	+ 6
Developing countries [3]	10 218	+ 9.5	+ 8.5	+ 14.5	+ 12	+ 12
including :						
Associated overseas countries and territories	2 295	+ 11	+ 31.5	+ 39	+ 50	+ 40
Other countries [4]	3 413	+ 10	+ 18	+ 12.5	+ .	+ 15

Source : Statistical Office of the European Communities (SOEC).

[1] 1 u.a. = 1 unit of account = 0.888671 g of fine gold = US $1 at the official exchange rate.
[2] Class 1 of the Standard Country Classification for Foreign Trade Statistics of the EEC.
[3] Class 2 of the Standard Country Classification for Foreign Trade Statistics of the EEC.
[4] Class 3 of the Standard Country Classification for Foreign Trade Statistics of the EEC, and other destinations.
[5] Estimates.

materials encouraged this tendency. To judge by the results of the EEC business survey, however, the fall in stocks held by manufacturers and dealers must in some sectors be set against involuntary stockbuilding by producers, the result being that the conflicting movements in stocks at the different levels partly offset each other.

The pattern of economic activity in the Community in 1970 was increasingly determined by the upward trend of *consumption.*

Public current expenditure on goods and services expanded at much the same pace as in 1969 (11 %); important contributing factors were the increase in public service salaries and, in some countries, a vigorous rise in the purchase of materials.

Private consumers' expenditure, which had already advanced with unusual vigour in 1969, continued to expand very rapidly. In terms of value its growth even gathered additional momentum. In terms of volume, however, the rise was of the same order as the year before, since the persistent strains in the business situation sent average consumer prices for the Community up more strongly than the previous year.

The key to the rapid advance in expenditure by households was the continued rapid increase in incomes. Wage incomes, for instance, rose at an unusually vigorous pace until the end of the year, the average advance for the year ranging from 10 % to 20 % in all Member States.

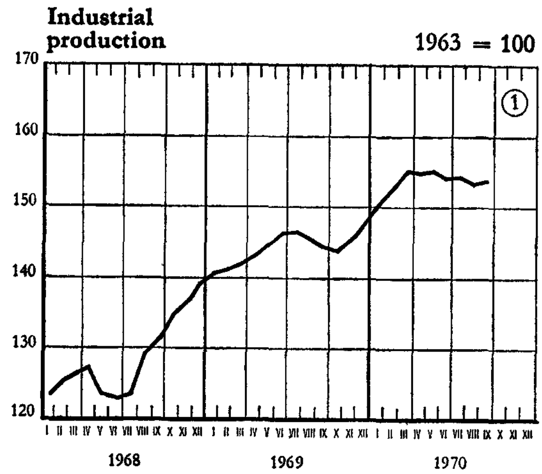
While transfer incomes continued to increase fairly appreciably, the rise in incomes from entrepreneurship and property probably slowed down in 1970. Savings activity, unlike the trend in incomes, varied fairly sharply from one country to another. While the propensity to save weakened appreciably in Germany and the Netherlands, the savings ratio went up in France, Italy and Belgium, notably in the first half of the year; in France, the advance was indeed sufficiently strong for the expansion of expenditure on consumption to be initially very calm and regain vigour only in the second half of the year.

3. Production and employment

The upward trend of *internal supply* in the Community, which was still very vigorous in 1969, slowed down distinctly during 1970. In most member countries this was mainly a result of the extremely high degree of capacity utilization and the acute labour shortage. In individual sectors however—particularly certain basic materials industries and textiles—the expansion of production was also dampened by the cautious stockbuilding policy of dealers and manufacturers, to which reference has already been made.

Agricultural production made only a very small contribution to the growth of internal supply in the Community. The information so far available shows that output of crop products did not rise appreciably compared with that for 1969. The grain harvest in the Community as a whole was probably some 6 % lower than last year, though other crops, for instance potatoes and sugar beet, were up, and the wine harvest should have been particularly plentiful. Output of livestock products on the whole advanced appreciably in almost all member countries, to judge by the figures on the trend in the first half of the year.

As in the previous year, *industrial production* (as defined by the Statistical Office of the European Communities, i.e. excluding construction and food, beverages and tobacco) expanded more strongly than output in the other sectors of the economy, even though its growth slowed down, both in terms of the trend and on a year-to-year comparison. From 1969 to 1970 it rose by some 8 %, compared with 11.7 % the year before; during the first half of 1970 the tendency was still distinctly expansionary, but it subsequently fell off significantly for the reasons set out above.



The trend varied sharply from one country and sector to another. In Italy, for instance, production recovered in the second half of the year while in the first half it had still been impeded by the unsettled social climate; in other member countries, especially Germany, it slowed down distinctly during the year.

Production expanded at a particularly rapid pace in the capital goods industries, while in most basic materials and some consumer goods industries a slackening in the flow of new orders became evident. This is especially true of the iron and steel industry, where production in some enterprises has actually declined since the end of the summer owing to the downward tendency of the stocks of dealers and final buyers.

In building and construction, a year-to-year comparison shows that the growth in real value added slackened distinctly, particularly in Germany and France. In Germany, this was due to the bad weather at the beginning of the year and the acute labour shortage; in France on the other hand to the weaker expansion of demand.

Activity in the *services sector* appears to have advanced at a lively pace. As in the previous year, particular vigour was shown by the sectors at or near the consumer stage, especially tourism and the distributive trades. The expansion of goods transport was hampered by the compara-

Industrial production in the Community

(% change on preceding year)[1]

	1968	1969	1969 3rd quarter	1969 4th quarter	1970 1st quarter	1970 2nd quarter	1970 3rd quarter
Industry as a whole [3]	+ 8.8	+ 11.7	+ 9.7	+ 6.3	+ 9.8	+ 6.2	+ 5 [2]
of which:							
Germany	+ 13.1	+ 13.8	+ 11.9	+ 11.6	+ 11.3	+ 7,7	+ 5.3
France	+ 4.0	+ 13.5	+ 9.0	+ 4.6	+ 8.5	+ 4.7	+ 3.9
Italy	+ 6.3	+ 2.8	+ 3.1	— 8.7	+ 5.5	+ 1.2	+ 3.8
Netherlands	+ 12.0	+ 13.5	+ 13.6	+ 13.4	+ 13.5	+ 10.7	+ 9 [2]
Belgium	+ 6.4	+ 10.9	+ 7.7	+ 10.8	+ 11.5	+ 8.5	+ 8 [2]
Luxembourg	+ 5.5	+ 13.4	+ 12.6	+ 11.5	+ 6.6	+ 5.1	— 0.9
of which:							
Mining and quarrying	+ 4.3	+ 4.1	+ 2.6	+ 2.2	+ 7 [2]	+ 1.5[2]	.
Textiles	+ 9.2	+ 9.0	+ 5.2	+ 4.9	+ 2 [2]	+ 0.5[2]	.
Paper and paperboard	+ 7.6	+ 10.7	+ 9.5	+ 8.4	+ 7 [2]	+ 6 [2]	.
Leather	+ 9.9	+ 5 [2]	— 0.3	— 2.5[2]	— 3 [2]	— 4 [2]	.
Metalworking	+ 7.3	+ 14.1	+ 11.8	+ 6.8	+ 11.9	+ 5.9	.
Iron and steel	+ 9.7	+ 8.8	+ 6.9	+ 3.7	+ 3.5	+ 5.4	+ 3.3
Electricity	+ 8.4	+ 10.2	+ 9.3	+ 8.4	0	+ 8.4	.

[1] Calculated on the basis of the unadjusted indices of the Statistical Offices of the European Communities.
[2] Estimates.
[3] Excluding construction and food, beverages and tobacco.

tively weak trend in building and the basic materials industries.

All in all, the real *gross Community product* may have expanded by some 6 % from 1969 to 1970, following an advance of 7.1% the previous year.

As had been expected, the slowdown of general economic growth was accompanied in the Community as a whole by a decline in *productivity* gains (gross value added at constant prices per person gainfully employed); following the comparatively sharp advances in productivity of the previous years, the pace now reached can be considered to be normal.

As in the previous year, the total number of persons employed showed a further slight rise from 1969 to 1970, in annual average terms. The number of *self-employed* declined further; the strong upward thrust of wages and the efforts made to form larger enterprises, particularly in the distributive trades, no doubt helped to strengthen the tendency towards an increase in the proportion of persons in paid employment and towards a fall in the proportion of self-employed in the gainfully employed population. All in all, the number of *persons in paid employment* in the Community probably rose at much the same rate as in 1969, i.e. by 2 %; the increase occurred mainly in industry and the services sector, while farming registered a fall.

All in all, the shortage of manpower, which has reached particularly serious proportions in the most heavily industrialized areas of the Community, was very pronounced in 1970. Compared with the previous year, the number of *unemployed* declined slightly in all member countries except France. Since the summer, when in several countries it was down to a level that can hardly be reduced any further, it has, however, been more or less stagnating. In October 1970, the unemployment rate was 0.6 % in Germany, 1.1 % in the Netherlands, and 1.8 % in Belgium; in September, it was 1.4 % in France; in August, it was 4.6 % in Italy.

4. Balance of the markets

The Community's *imports* from non-member countries again expanded briskly in 1970. In terms of value, the average rise over the year was 17 %, the same as in 1969. In terms of volume, the advance was 13 ½ %, as against 15 ½ % in 1969. The proportion of imports in the supply of goods in the Community has therefore continued to grow significantly.

The very dynamic trend in imports is mainly attributable to the appreciable expansion of economic activity and to the strains on most markets for goods in the Community. The very lively advance in corporate investment, for instance, led to a rapid increase in imports of plant and machinery. Bottlenecks in the production of certain consumer goods also resulted in an increasing switch to imports. In some countries, substantial raw material requirements sent raw material imports up vigorously, especially in the first half of the year, when the appreciable rise in the price of petroleum in the spring entailed a rapid increase in the value of fuel imports. Less favourable harvests in 1969 and the persisting rise in world market prices for a large number of foodstuffs made the value of foodstuff purchases go up appreciably.

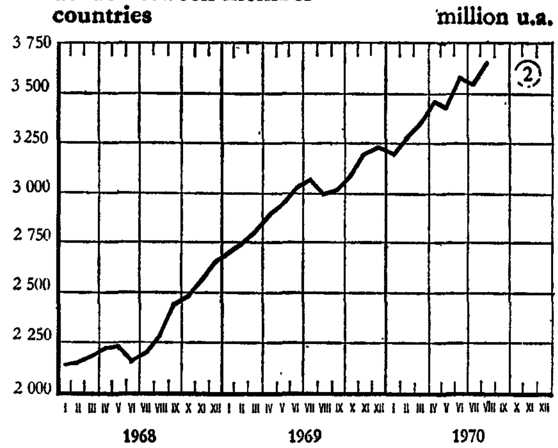
Deliveries by the United States benefited particularly strongly from the buoyancy of imports into the Community; from 1969 to 1970, their value probably went up by almost one third.

Sales by the EFTA countries to the Community, which had already shown a lively rise in 1969, continued to expand rapidly in 1970. Deliveries by the Mediterranean countries, especially Spain, Yugoslavia, Greece and Turkey, climbed considerably. The developing countries also stepped up their exports to the Community; from 1969 to 1970, deliveries by the overseas associated countries, for instance, went up by almost 30 %.

The state-trading countries increased their sales to the Community at about the same pace as last year (15 %).

Although *intra-Community trade* was still expanding in 1970, the rise tended to be weaker than in 1969; on the basis of import statistics, the increase in terms of value was 20 % (compared with 28 % the previous year). In contrast to developments in the previous years, it was therefore only slightly higher than the advance in imports from non-member countries. The main reason for this, no doubt, was the greater elasticity of supply from some non-member countries. The slowdown in expansion of trade between member countries is in part also accounted for by the considerable slowdown in trade in agricultural products, which had been inflated in 1969 by speculation. Another important factor was probably the delay in exports from Italy as a result of the persistent social unrest there. An analysis of the development of intra-Community trade, as shown by the imports figures, suggests that the restraining effect of the devaluation of the French franc, and of the stabilization process decided upon by the Government, was very sharp, while the revaluation of the German mark appears to have stimulated German imports only to a limited extent so far. On the export side, the growth in the volume of Germany's and Italy's exports proves to have slowed down appreciably—in

Trade between member countries million u.a.



the case of Italy, in connection with the stoppages; by and large, the influence of these movements was stronger than the acceleration in French exports resulting from the parity change.

Visible imports from non-member countries

(Imports 1969 and % year-to-year changes)

	1969		1970			
	Million u.a. [1]	Full year	1st quarter	2nd quartter	3rd quarter [5]	Full year [5]
All non-member countries	39 242	+ 17	+ 17.5	+ 17.5	+ 17	+ 17
of which :						
Industrialized countries [2]	22 236	+ 19.5	+ 23.5	+ 19.5	+ 19	+ 20
including :						
United States	7 326	+ 14.5	+ 41	+ 19.5	+ 19	+ 26
EFTA	9 450	+ 20.5	+ 11.5	+ 16.5	+ 14	+ 14
United Kingdom	3 588	+ 19.5	+ 11.5	+ 17.5	+ 5	+ 12
Developing countries [3]	14 222	+ 13.5	+ 9.5	+ 14.5	+ 16	+ 13
including :						
Associated overseas countries and territories	2 807	+ 12.5	+ 31.5	+ 28	+ 31	+ 30
Central and South America	3 166	+ 18	+ 7	+ 23	+ 17	+ 16
Other countries [4]	2 784	+ 15.5	+ 15.5	+ 13	.	+ 15

Source : Statistical Office of the European Communities (SOEC).

[1] 1 u.a. = 1 unit of account = 0.888671 g of fine gold = US $1 at the official exchange rate.

[2] Class 1 of the Standard Country Classification for Foreign Trade Statistics of the EEC.

[3] Class 2 of the Standard Country Classification for Foreign Trade Statistics of the EEC.

[4] Class 3 of the Standard Country Classification for Foreign Trade Statistics of the EEC and other sources.

[5] Estimates.

Except in Italy, the growth of exports by member countries to all other Community countries again showed a comparatively homogeneous pattern in 1970. Despite a certain slowdown in the second half of the year, sales by the Netherlands registered the strongest advance, especially as a result of the rapid upswing in deliveries to Germany, which accounted for almost 50 % of total Netherlands exports to Community countries. The vigorous expansion in Italian imports caused sales by France to rise appreciably.

As regards the trend of the individual member countries' balances of trade with the other Community countries, the main features are a reversal of the trend in France and Germany and a sharp deterioration in the position of Italy. The French balance of trade, which had deteriorated constantly since 1966, recovered considerably in 1970. The deficit fell to some 700 million units of account and was thus down to half the figure for the year before, while in Germany the trade surplus diminished appreciably, although this movement was nothing like as sharp as the improvement in the French position. The balance on Italy's trade account, which was still in surplus in 1969, deteriorated very markedly (by some 700 million units of account). The distinct improvement in the situation of the Belgo-Luxembourg Economic Union, recorded for four successive years, continued. The surplus mounted to a record level of 1 300 million units of account. The Netherlands balance of trade also improved; for the first time since 1958 it was almost in equilibrium.

The deterioration in the conditions which determine the balance in the Community is mainly reflected in a very vigorous rise in the *price level.* Prices were soaring in all member countries. From 1969 to 1970, the rise was even greater than a year earlier; this applies to consumer goods, and still more to investment, particularly in building and construction.

In contrast to the situation in 1969, external factors contributed little if anything to the rise in prices in the Community. Since the spring of 1970, the upward tendency of world market prices for most industrial raw materials has given way to a fairly distinct fall, with the important exception of petroleum prices, which continued to rise sharply. World market prices for agricultural products also climbed further, but as, under the common agricultural policy, the levies on a large number of products are reduced in such a case, this upward movement had practically no effect on prices in the Community.

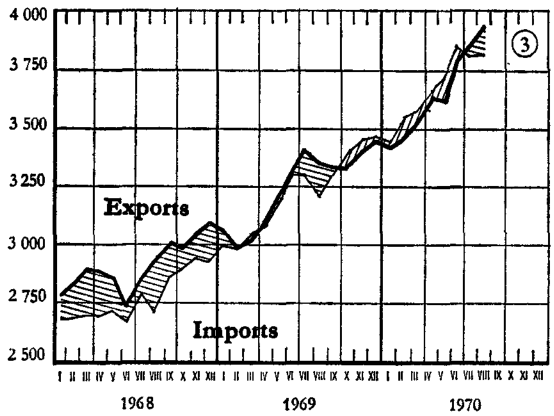
Prices for services and finished industrial goods produced in the Community continued, on the other hand, to tend strongly upwards. In most countries the key to this tendency was the strained demand/supply relationship, but the very vigorous rise in costs also contributed more and more to the upward trend. Generally speaking, there were still no signs of moderation in the inflationary behaviour of transactors.

The rise in labour costs per unit of output gathered momentum in most Community countries. This was not only because wages continued to go up vigorously, but also because productivity gains were shrinking. Managements for their part endeavoured to pass on higher costs to their customers as fully as possible by putting up prices.

The changeover to VAT in Luxembourg and the increase in a large number of rates of indirect taxes in Italy were autonomous factors that contributed additional vigour to the wave of price increases in these countries.

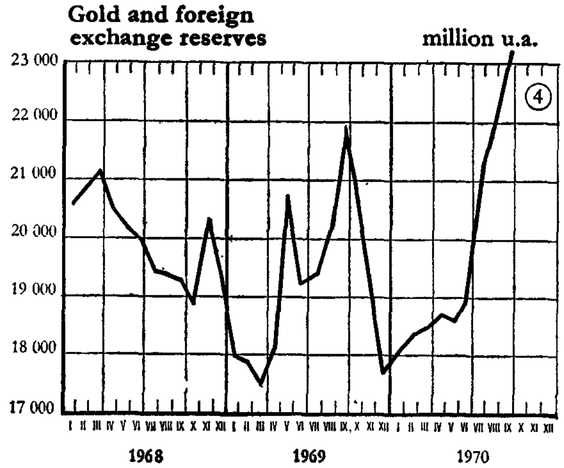
The tendency, observed since 1968, for the Community's *balance of visible trade* (cif-fob) with the non-member countries to deteriorate continued in 1970. Whereas in 1969 the balance of trade showed a deficit of $6 million and was thus virtually in equilibrium, 1970 may have brought a deficit of some $1 400 million. The surplus on the Community's *current account* is likely to fall accordingly.

Trade with non-member countries million u.a.



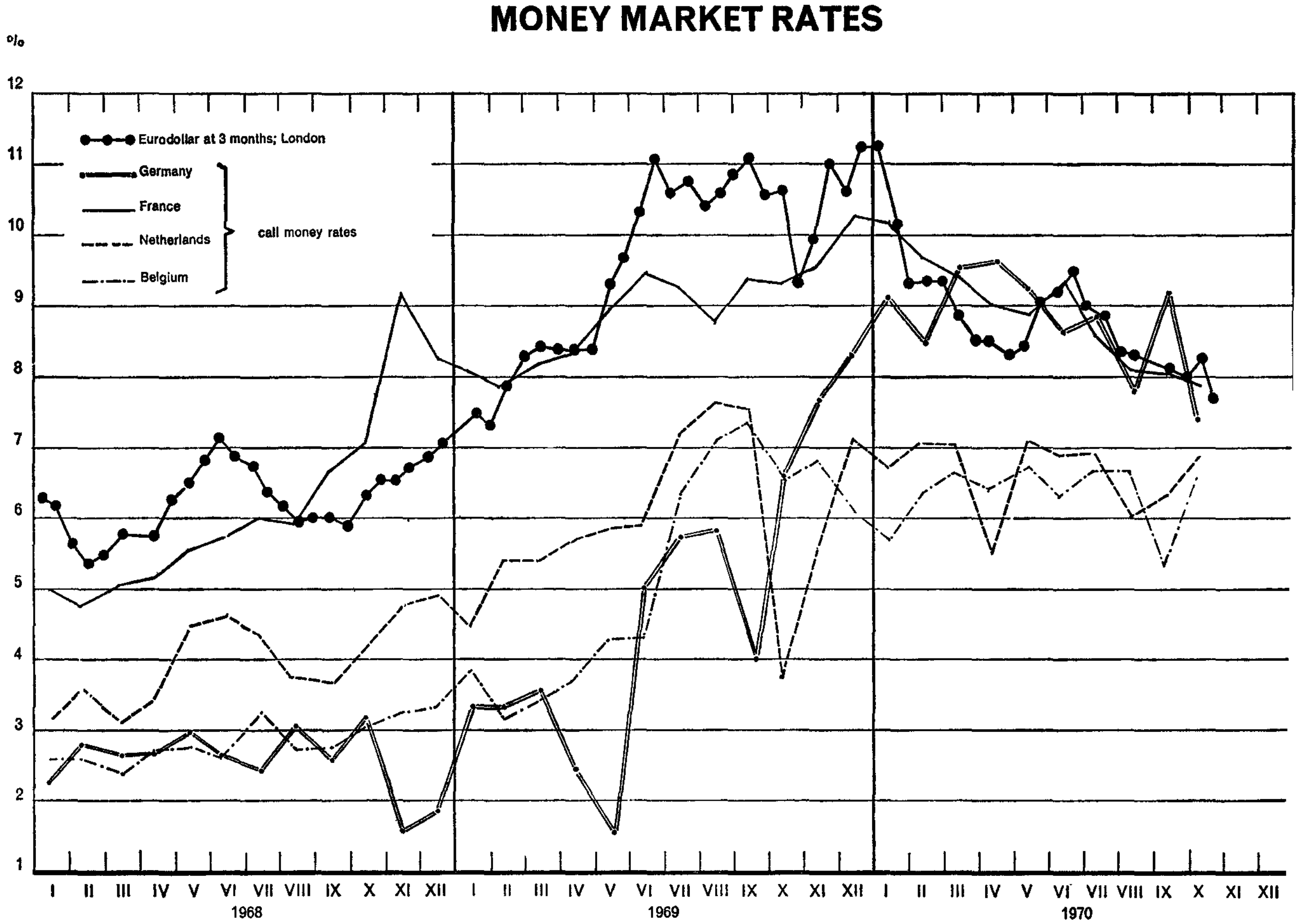
The Community's *capital account,* on the other hand, was in surplus, in contrast to the situation last year. Long-term capital transactions, which in 1969 had registered a heavy deficit, may have been almost in balance in 1970. Net imports of short-term funds, on the other hand, continued to expand vigorously. There are several reasons for this distinct reversal in the capital account: in all countries a major part was undoubtedly played by the restrictive monetary and credit policy, which considerably reduced the possibilities for obtaining finance within the country and also kept the level of interest rates in the Community very high at first, whereas rates on the Euro-dollar market had fallen distinctly at the beginning of the year and again since the summer. After the rate of exchange of the Canadian dollar had been allowed to float, there were also speculative inflows of foreign exchange into Germany and, to a lesser extent, into the Netherlands. Several Member States have cut their discount rates since the summer with a view to checking the inflow of foreign exchange that expanded domestic liquidity. In Italy, where exports of capital reached unusually large proportions for a time, the measures taken by the Government and the monetary authorities have caused the position of the lira to become firmer again since August. France's capital account reflected the renewed confidence in the franc, prompting the Banque de France to ease the foreign exchange regulations a little in the summer. With statistical data on capital movements within the Community still missing at the time of completion of this Survey, it is practically impossible to analyse the flows of capital within the Community. Generally speaking, however, it is safe to say that capital movements, which had a considerable unsettling influence in the Community in 1969, were much more balanced in 1970.

Official *gross gold and foreign exchange reserves* in the Community rose significantly. In the first ten months, the increase was about \$6 800 million, which compares with a fall of \$1 700 million for 1969 as a whole. At the same time, however, there was an appreciable deterioration in the foreign exchange position of the commercial banks, particularly in Germany.



The *cash transactions of the public authorities* reflected the efforts of governments to dampen excessive activity by budget policy measures. In

MONEY MARKET RATES



France, the budget for 1970 was in equilibrium, in accordance with the stabilization programme introduced in 1969. The cash position is also likely to have been in equilibrium at the end of 1970, following heavy surpluses in the first half of the year. In Germany, the Federal budget was planned to yield a surplus of DM 1 600 million, which was to be deposited in full with the Bundesbank as a counter-cyclical equalization reserve. However, with considerable expenditure to meet that was still to be charged against the previous year, and with tax receipts falling short of expectations, cash operations for 1970 were probably at best in equilibrium, whereas in 1969 there had been a surplus of DM 1 500 million. The budgets of the Länder are also unlikely to have closed with as favourable a balance as last year. In the Netherlands, the central government's budget deficit was almost Fl. 3 000 million, which is one third more than originally planned, but in contrast to 1969 only a very small part of it was financed via the money market. In Belgium, where the previous years had brought deficits, the cash operations under the ordinary budget probably closed with a small surplus, mainly

Demand for and supply of goods and services

	1968 [1]	1969 [2] [5]		1970 [3] [6]		1971 [4] [6]
	At current prices in '000 million u.a.[7]	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Gross fixed asset formation	88.9	+ 9.2	+ 15.6	+ 8	+ 18	+ 5½
Public current expenditure on goods and services	54.2	+ 3.9	+ 11.0	+ 3	+ 11½	+ 4½
Private consumers' expenditure	228.9	+ 6.9	+ 11.4	+ 7	+ 12	+ 5½
Gross Community product	384.2	+ 7.1	+ 12.4	+ 6	+ 12½	+ 4½
Balance exports less imports (in '000 million units of account) [7]	+ 7.1		+ 5.3		+ 4.8	+ 4.3

[1] Statistical Office of the European Communities; General Statistics (monthly bulletin) 1970, No. 10.
[2] Actual results.
[3] Estimates.
[4] Forecasts.
[5] Based on Community totals of the aggregates of the individual member countries at official exchange rates 1963.
[6] Based on Community totals of the aggregates of the individual member countries at official exchange rates 1970.
[7] 1 u.a. = 1 unit of account = 0.888671 g of fine gold = US \$1 at the official exchange rate.

Note :

(a) The difference between the figures for demand and those for supply is accounted for by movements in stocks and differences in treatment of the balance of exports less imports.

(b) The estimates and forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with the experts of the member countries but are established and published on the sole responsibility of the Commission.

because tax receipts were higher than expected. Most of the deficit on the extraordinary budget was financed through loans. Only the Italian budget had a strongly expansionary influence on domestic liquidity, at least until the beginning of the autumn. This country's cash deficit from January to July was more than six times heavier than a year earlier. By the end of the year, the cash position may have improved again, as a result of the tax increases agreed in August and because the arrears in tax receipts due to a sluggish inflow at the beginning of the year have been made good.

Bank lending to business and private customers continued to expand very sharply, even though the pace in all member countries was no longer as rapid as a year earlier, at least until the end of the summer. The monetary authorities of all member countries endeavoured to contain the expansion of credit on the supply side by means of monetary and credit restrictions. In certain cases these efforts were considerably impeded by massive inflows of foreign exchange. After the level of interest rates outside the Community, notably on the Euro-money markets, had fallen appreciably in the summer, Germany, France and Belgium cut their discount rates, which until then had been the highest in the Community.

The *volume of money* expanded very powerfully in the Community as a whole. At the end of August it was some 14 % up on the level of a year earlier. Only in France and Belgium was the rise in the money supply decidedly weak. In most member countries, the rise was engendered by bank lending and transactions with abroad. In Italy, however, it was the direct or indirect financing of the public authorities by the Central Bank that led to a sharp increase in liquidity. The formation of monetary capital declined in almost all member countries, in line with what had been observed in earlier phases of overheating. Only in France did the propensity to long-term saving increase distinctly.

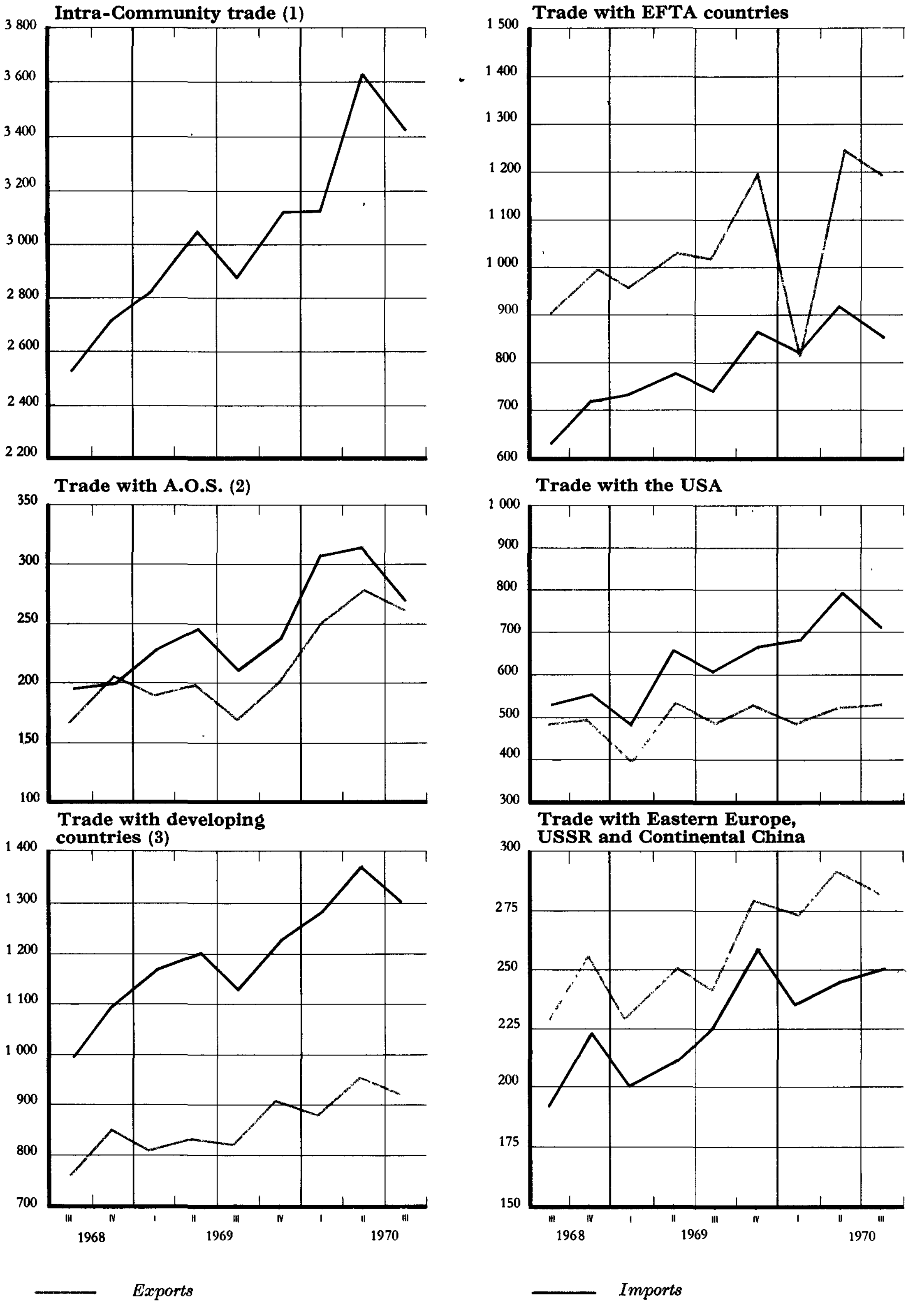
Despite the credit restrictions, the situation on the Community's *money markets* eased perceptibly in the course of the year. The fall in Euro-dollar rates and the inflows of money largely attributable to it no doubt contributed largely to this development. At the beginning of 1970, credit policy in the United States was eased cautiously, enabling American banks to repay during the year part of the funds they had raised on the Euro-market. But the downward trend of interest rates which this touched off on the Euro-market was impeded through heavy calls on this market by German banks and German and Italian enterprises. Following the relaxation of Regulation Q (upper limit on the rate of interest which banks can pay on time deposits) in the United States on 24 June, interest rates on the Euro-money market fell more strongly again, gradually leading to a downward tendency of interest rates on the Community's money markets as well. The German Bundesbank, the Banque de France and the Banque Nationale de Belgique followed this trend and cut their discount rates.

On the *capital markets* of the Community the situation has also eased somewhat since the middle of the year. On the bond markets the trend of interest rates appears to have passed its peak in the summer. This is in line with developments in the United States and for Euro-issues. Belgium is the only country where there has been no distinct tendency for interest rates to fall. However, yields there had previously risen less strongly. Share prices, which had been falling for quite some time owing to the restrictive credit policy, and which in May had dropped sharply owing to a strong downturn in prices on the New York Stock Exchange, have been recovering somewhat since the summer in almost all member countries.

COMMUNITY TRADE

Monthly averages

In million u. a.*



(1) According to import returns.
(2) A.O.S. : Associated Overseas States (overseas departments, countries and territories).
(3) According to GATT classification : non-industrialized regions other than A.O.S.
* 1 unit of account = 0.888671 gramme of fine gold.

Some of the data for the third quarter of 1970 are estimates only.

B. Forecasts for 1971

The world economic trend in 1971 will differ distinctly from that which prevailed during most of 1970. A revival of economic growth in the United States, Canada and the United Kingdom is likely to contrast with an appreciable slowdown in expansion in the Community and the rest of continental Europe. Generally speaking, world trade in 1971 should be stimulated by the next series of tariff cuts, due to be made at the beginning of the year under the Kennedy Round agreements in GATT, unless major world trading countries resort to protectionist measures.

In the *United States,* the revival in economic activity which began to emerge in the third quarter of 1970 but was interrupted in the fourth quarter by the strike in the motor industry, is likely to continue in 1971 and will probably gain in strength. The main stimulus will presumably come from the expansion of private consumers' expenditure. Pointers in this direction are the additional tax alleviations decided upon at the end of 1969 under the reform of direct taxation, the probable return to normal of the hitherto comparatively high savings ratio, and a stabilization of the level of employment in the course of the year. The recovery is also likely to continue in residential construction, and stockbuilding too should have a less inhibiting effect on the expansion of economic activity, particularly if steel consumers build up their stocks substantially, owing to fears that the steel industry may be faced with a labour dispute in the summer of 1971. The rise in corporate investment, on the other hand, will probably be weak during the greater part of the year.

All in all, the real gross national product for 1971 as a whole may rise by 3 ½ %, particularly if further efforts are made at the beginning of 1971 to make good at least part of the losses of production caused by strikes. The propensity to import may be comparatively weak in 1971, despite the recovery in economic activity. There is, to be sure, considerable uncertainty about the level of imports of plant and machinery and consumer goods, which rose vigorously in 1970 although the real gross national product was declining. In addition, it is quite on the cards that in the first half of the year fears of a strike in the American steel industry will lead to an expansion in steel imports. The rise in prices will probably slow down further.

In the *United Kingdom,* the immediate and longer-term effects of the substantial wage increases will continue to stimulate private consumers' expenditure, at least during the first half of 1971. Residential construction may also expand vigorously in 1971. Corporate investment however will, to judge by the latest surveys, show little if any increase in terms of volume, while the stimuli provided by exports may be comparatively weak, owing to the developments to be expected on the country's main export markets. The interim budget which the Government submitted in October, and which inter alia provides for an immediate cut in corporation tax, a cut in income tax from April 1971, the replacement of investment grants by a system allowing faster depreciation and the reduction of certain items of public expenditure below the figures set out in the original budget, will probably be broadly neutral in its effect on incomes and demand. At the same time, the monetary authorities raised minimum reserve rates, thus confirming their intention to maintain the restrictive line of monetary and credit policy in the months ahead. Nevertheless, the expansion of economic activity, which picked up in the second half of 1970, is likely to continue in 1971, boosted by the dynamic trend of private consumers' expenditure. For the full year, real gross national product may be up by 3 %. The upward thrust of prices may remain vigorous. With expansion gathering momentum, imports are likely to go up more rapidly than they did from 1969 to 1970. One of the reasons for this is that the import deposit scheme will be completely eliminated in December 1970, and importers may postpone purchases beyond this deadline, so that imports will presumably rise more vigorously at the beginning of 1971.

In most *continental EFTA countries,* economic activity will undoubtedly slacken in 1971. In the Scandinavian countries in particular, the calming-down expected for the end of 1970 will probably be still more pronounced in the first half of the new year, particularly since the measures taken in these countries to combat inflation and restore external equilibrium were appreciably reinforced in the autumn of 1970. All in all, real growth in these countries will therefore be distinctly weaker than in 1970, and the propensity to import will probably decline appreciably in all of them except Norway, where investment programmes provide for a sharp increase in the purchase of ships.

In the other industrial countries, economic activity must on the whole also be expected to weaken—if it changes at all.

Even though there is reason to believe that in 1971 the expansionary tendency of imports by the *developing countries* will be weaker than in 1970, it is very difficult to say what proportions the slowdown will assume. The slackening in the growth of imports by the Community and the EFTA countries, and in smaller measure also by Japan, must be expected to outweigh the revival in raw material imports by the United States. The decline in prices for the most important raw materials is at the same time likely to have a negative impact on the export earnings of the developing countries. These factors, coupled with what will probably be only a weak rise in development aid, may have an unfavourable influence on the imports of the countries which produce basic materials. As these countries have, however, been able to build up their foreign exchange reserves significantly in recent years, their imports may nevertheless run at a comparatively high level in 1971.

On the basis of these assumptions, the increase in world trade from 1970 to 1971, including EEC member countries' imports from each other and from non-member countries but excluding imports by the state-trading countries, can be estimated at 10 %, in terms of value. In terms of volume, the rise will probably be 8 %, not very much less than the advance from 1969 to 1970, since the rise in prices will presumably be considerably weaker. If imports by the EEC countries and the state-trading countries are left out of account, world trade in 1971 should rise by 9 % in terms of value.

In these circumstances it can be assumed that the expansion of the Community's exports to non-member countries will fall off appreciably in 1971. The growth of sales to the industrial countries and particularly the continental EFTA countries will indeed slow down very distinctly. Deliveries to the developing countries are also likely to show a considerably weaker advance than in 1970. Even assuming that the trend in sales to the state-trading countries will continue to be satisfactory, the growth of Community exports to non-member countries is in the aggregate not likely to exceed 8 % in terms of value, as against 14 % in 1970. In terms of volume, these exports may rise by some 6 ½ %, compared with 9 % in 1970.

Internal demand in the Community will presumably continue to rise at a lively pace in 1971, even though distinctly more slowly than in 1970.

Gross fixed asset formation in particular will probably expand at an appreciably weaker rate than in 1970.

This is true in particular of corporate *investment in plant and machinery.* Admittedly, as order books are well filled, actual investment activity can be expected to go on rising appreciably, at least during the early months of 1971, but in some member countries there is, to judge by the trend of new orders in the capital goods industries, already unmistakable evidence of a decline in managements previously very brisk propensity to invest. The rapid increase in wage costs and the prospect of further appreciable wage increases in 1971, together with the fact that on markets where the tendency is not as distinctly upwards the rise in costs is probably more difficult to pass on to prices, suggest that in 1971 enterprises will have only limited scope for self-financing. In some member countries, self-financing was already made more difficult in 1970 by special measures concerning depreciation. The restrictive monetary and credit policy that is being pursued in all member countries limits the possibilities for borrowing. In addition, capacities in some branches have been expanded so vigorously as to make it by no means always possible to ensure optimum utilization immediately, a circumstance which will probably prompt managements to be more cautious when considering the creation of further capacity. However, the change in the investment climate varies fairly widely from one member country to another; in France and Italy, there is as yet little evidence of it, while in Germany and the Benelux countries it is very pronounced.

Annual average growth of *expenditure on building and construction* is likely to weaken further in 1971, continuing the tendency already observed during 1970. The acute labour shortage recorded in 1970 and the unusually sharp rise in building costs will probably be eased only slowly and therefore continue to be major inhibiting factors, especially where the volume of building activity, and especially residential construction, is concerned. In Italy, activity in the latter field may, in fact, tend distinctly downwards.

In industrial building, the growth of actual spending will probably slow down during 1971, as the projects started the previous year reach completion, because the increase in new building projects will be weaker than in 1970, for much the same reasons as with investment in plant and machinery.

In public works, expansion in terms of value is likely to gather a little momentum, to judge by the information available on the budgets; in terms of volume, however, growth will probably be very limited, given the persistent rise in costs.

Stockbuilding, on the other hand, may provide somewhat more vigorous stimuli again in 1971. The tendency to run down stocks, observed in the Community during the second half of 1970 particularly in respect of basic materials and semi-manufactures, will probably come to a halt in 1971. Given the high cost of credit, however, enterprises will no doubt tend to keep the ratio of stocks to turnover as low as possible.

Consumption will still display a very pronounced upward trend throughout most of 1971, even though total spending will no longer grow as rapidly as in 1970.

To judge by the draft budgets of the member countries, public current expenditure on goods and services should continue to rise fairly vigorously. Important factors here are the expected increase in public service wages and salaries and the more rapid increase in certain types of expenditure on materials.

Private consumers' expenditure will likewise expand very rapidly, even though the pace will be distinctly weaker than the previous year. According to estimates by the Commission departments, the rise can at present be expected to be 10 %, as against 12 % in 1970.

It is in fact reasonable to assume that all member countries will be faced with a further considerable rise in the wages bill, which is the most important component of gross incomes of households. During the year, however, the gap between agreed wages and actual earnings may narrow. The rise in the wages bill will also be influenced by a weaker rise in employment and a shortening of hours actually worked.

While the increase in transfer incomes can be expected to be of the same order as in 1970, the less favourable profit trend in 1970 and the probable further narrowing of corporate profit margins in 1971 point to a weakening in incomes from entrepreneurship and property.

Part of the rise in gross incomes will in most member countries undoubtedly be absorbed by higher tax rates under the progressive scale, especially in Germany, where a surcharge on income taxes will be levied until the middle of 1971, and in the Netherlands, where the Government intends to raise the rates of income tax by 3 %. In France, on the other hand, the effects of the progressive tax scale are partly offset by income tax concessions amounting to FF 3 200 million.

In most member countries there is some measure of uncertainty about the future trend in the savings ratio, which may, if anything, decline again, especially in France and Italy, where it rose substantially in 1970.

Internal supply in the Community will initially not be able to keep up with the still comparatively vigorous expansion of demand. The Commission departments currently assume that the real gross Community product will rise by 4 ½ % from 1970 to 1971, as against 6 % in 1970. In connection with this slower growth rate, however, it is of considerable importance to note that the figures for production reached at the end of 1970 were, after adjustment, appreciably less above the average for the year than at the end of 1969—which means that in relation to the figures at the end of the previous year the slackening of expansion will be decidedly smaller. Nevertheless it should be realized that while some industries will still run at or near capacity, particularly in the first half of the year, others will be faced with a temporary decline in production and will therefore operate below capacity. This is partly the result of an excessive investment boom in most member countries in past years, during which there was some tendency to overestimate future sales possibilities, particularly because of the impetus which rising prices gave to the expansion of demand.

After several years of very substantial advances in productivity there will probably be a slackening in productivity gains, partly because enterprises, though faced with a decline in demand, may refrain from dismissing labour, because of the persistent manpower shortage.

When it is also borne in mind that reductions will be made in statutory and agreed hours of work, the expected growth is likely to ensure maintenance of full employment. In 1971, structural imbalances may, however, again make themselves felt more strongly on the labour markets, especially in the skills and the geographical pattern of available manpower in relation to the requirements of trade and industry.

The prospective trends of production and overall demand, and the ratio of internal supply to overall demand, suggest that the rise in Community *imports* from non-member countries will be weaker from 1970 to 1971 than from 1969 to 1970. The loss in vigour of industrial production will mainly affect imports of raw materials and intermediate products.

The rise in imports of plant and machinery will also be hampered by the change in the investment climate. Purchases of consumer goods, however, will still expand at a fairly rapid pace. On balance, imports will still rise more strongly than exports from one year to the other, leading to a further deterioration in the balance of trade, particularly in the first half of the year.

The *price climate* will, on the whole, still be fairly strained, although the spate of price increases may already have passed its peak in most member countries. Even if the strains between supply and demand ease appreciably, the hitherto unusually vigorous rise in costs will still make for a very appreciable upward thrust of prices, since experience gained in late phases of economic cycles indicates that this rise is likely to persist for a while, although it may lose in vigour. In this connection it must also be borne in mind that in some member countries the prices of a number of products will have to be adjusted upwards owing to the strict price policy pursued by governments in recent years.

TABLE 1 : **Basic data 1969**

	Community	Germany	France	Italy	Netherlands	Belgium	Luxemburg (1)
Total area ('000 sq. km.)	1 167.5	248.5	551.2	301.2	33.5	30.5	2.6
Total population ('000)	188 147	60 842	50 345	54 090	12 873	(9660)	(337)
Density of population per sq. km.	161	245	91	176	384	(317)	(129)
Numbers in employment ('000)	74 196	26 822	19 967	18 871	4 625	3 772	138.8
Numbers in employment, breakdown by main sector (%) :							
— Agriculture	13	9.5	15.0	21.3	7.4	5.1	12.1
— Industry	44	48.2	40.6	42.7	40.2	42.5	45.3
— Services	43	42.3	44.4	36.0	52.4	52.4	42.6
Share of gross domestic product (%) :							
— Agriculture	.	4.3	5.8	11.3	7.0	5.3	5.3
— Industry	.	52.1	47.7	38.9	41.6	41.6	52.0
— Services	.	43.6	46.5	49.8	51.4	53.1	42.7
In % of gross domestic product :							
— Private consumers' expenditure	.	55.4	60.5	63.4	56.1	62.6	59.3
— Public current expenditure on goods and services	.	15.6	12.3	13.4	15.7	14.2	11.8
— Gross fixed asset formation	.	24.3	25.4	20.5	25.6	21.4	22.9
— Total exports	.	23.5	14.5	20.5	45.1	41.7	78.6
— Total imports	.	21.0	15.2	18.1	45.2	41.5	73.2

(1) 1968

TABLE 2 : **Key indicators**

	% change by volume on preceding year					Volume indices (1963 = 100)
	1965	1966	1967	1968	1969	1969
Gross Community product	4.9	4.3	3.2	5,9	7.1	136
Industrial production	4.1	5.0	1.4	8.8	11.6	144
Visible imports	5.0	6.8	0.6	11.5	16.0	156
Private customers' expenditure	5.0	4.7	3.7	4.9	6.9	134
Gross fixed asset formation	3.2	4.5	1.0	7.1	9.2	140
Visible exports	11.0	8.4	7.7	13.1	6.9	171
Intra-Community visible trade	12.2	10.9	6.1	18.9	22.6	218
Gross product per capita	3.6	3.4	2.6	5.3	6.3	129

Community

TABLE 3 : Basic monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1963 = 100)	1968	120	126	131	133	121	130	119	106	136	141	148	146
	1969	138	142	146	150	151	152	135	115	145	150	158	154
	1970	150	156	160	160	163	157	143	120				
Imports from non-member countries (cif, million u.a.)	1968	2 694	2 606	2 811	2 709	5 408		2 850	2 608	2 790	2 991	3 061	3 008
	1969	3 175	2 793	3 105	3 283	3 321	3 376	3 259	2 858	3 365	3 637	3 407	3 636
	1970	3 664	3 397	3 608	3 959	3 735	4 000	3 780	3 376				
Exports to non-member countries (fob, million u.a.)	1968	2 781	2 771	3 025	2 848	5 323		3 206	2 772	2 784	3 297	3 171	3 286
	1969	2 886	2 745	3 261	3 306	3 295	3 296	3 584	2 801	3 225	3 729	3 425	3 658
	1970	3 285	3 349	3 742	3 828	3 589	3 949	3 984	3 322				
Balance of trade (million u.a.)	1968	+ 87	+ 165	+ 214	+ 139	− 85		+ 356	+ 164	− 6	+ 306	+ 110	+ 278
	1969	− 289	− 48	+ 156	+ 23	− 26	− 80	+ 325	− 57	− 140	+ 92	+ 18	+ 22
	1970	− 379	− 48	+ 134	− 131	− 146	− 51	+ 204	− 54				
Intra-Community trade (million u.a.)	1968	2 123	2 162	2 371	2 287	4 248		2 479	2 085	2 409	2 773	2 658	2 724
	1969	2 696	2 727	3 057	3 043	3 013	3 101	3 157	2 415	3 089	3 554	3 144	3 242
	1970	3 140	3 284	3 604	3 782	3 247	3 861	3 655	2 949				

NOTES TO GRAPHS AND TABLES

Source: Community: Statistical Office of the European Communities (SOEC).
Germany: SOEC; Statistisches Bundesamt.
France: SOEC.
Italy: Relazione generale sulla situazione economico del Paese (1969).
Netherlands: SOEC; Ministerie van Sociale Zaken en Volksgezondheid; Centraal Bureau voor de Statistiek.
Belgium: SOEC; Ministère de l'emploi et du travail;
Luxembourg: SOEC.

Conversion into units of account (1 u.a. = 0.888671 g of fine gold = US \$1) at the official exchange rates.

Graph 1

— Three-month moving averages of the seasonally adjusted indices (excluding construction, food, beverages and tobacco).

Graph 2

— Three-month moving averages of the seasonally adjusted value of trade between member countries, as shown by foreign trade statistics on imports.

Graph 3

— Three-month moving averages of the seasonally adjusted value of exports to non-member countries (fob) and imports from these countries (cif), as shown by foreign trade statistics.

Graph 4

— Total gross reserves of gold and foreign exchange held by the monetary authorities of the member countries at the end of each month.

Table 1

- Total population at mid-year; for Germany, estimated average for year; for Italy, average for year.
- Resident population in employment at mid-year; for Germany, estimated average for year; for Italy, average for year less persons temporarily working abroad.
- Breakdown by agriculture, industry and services at factor cost; for Luxembourg, 1967 figures.
- Shares of the major aggregates in the gross domestic product at market prices.
- Total exports and imports: goods, services and factor income.

Table 2

- Industrial production: index of the Statistical Office of the European Communities, excluding construction, food, beverages and tobacco.
- Imports (cif) from non-member countries, as shown by foreign trade statistics.
- Exports (fob) to non-member countries, as shown by foreign trade statistics.
- Trade between member countries, as shown by foreign trade statistics on imports.

Table 3

- See note to Table 2.

II. THE SITUATION IN EACH OF THE COMMUNITY COUNTRIES

A. Germany

The year 1970 again saw vigorous economic expansion in Germany, though, in consequence of the recent revaluation, export demand was calmer and domestic demand came more and more to be the main growth factor. Orders for capital goods, in particular, mounted so steeply in the early months as to drive producer prices up faster than ever before. As elasticity of supply diminished, the German economy was thrown more and more out of balance, so that the existing restrictive policy, hitherto principally the affair of the Central Bank, had in mid-1970 to be supplemented by a government stabilization programme. In the second half of the year the inflow of orders decidedly lost momentum, but the danger of a further worsening in the price and cost situation continues to cloud the outlook.

In view of the sharp increase in incomes, 1971 will be marked by high consumer spending. Capital expenditure on the other hand, especially by enterprises, may be expected to rise noticeably more slowly, particularly because of narrower profit margins. Now that production capacity has been overstrained for some time elasticity of supply will be smaller, and therefore the growth in real gross national product, by some 3 ½ %, will be somewhat below the trend charted for the medium term. Nevertheless, stabilization of costs and prices should remain the foremost aim of short-term economic policy for the present.

1. Balance sheet for 1970

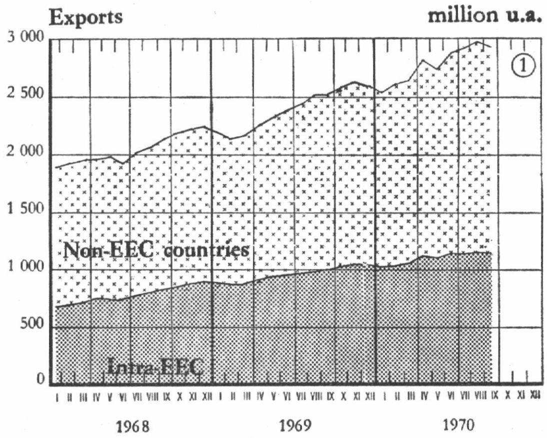
During most of 1970 the German economy was marked by considerable excess demand. The inflow of orders did slacken somewhat from the summer onwards, but to begin with this did no more than ease the strain, particularly as the elasticity of supply also decreased following the protracted overstretching of production capacity. Generally speaking, upward pressure on costs and prices continued to be very strong until the end of the year.

The pull of export demand diminished perceptibly as a result of revaluation and of a slight downturn in business activity in some major purchasing countries. The increase in visible exports (as defined for the national accounts) was 11%, a smaller rise, for the first time since 1962, than that in gross national product in terms of money. The fact that exports levelled off only gradually over the year although fewer orders were coming in was due mainly to the substantial backlog of orders. With prices rising abroad, it was even possible to put up export prices in marks notwithstanding the revaluation of the previous autumn.

The geographical pattern of export growth altered noticeably during 1970, owing partly to the differentiation of world business activity but also to the impact of the parity changes in 1969. Thus, sales to most of the other EEC countries, notably Italy and the Netherlands, increased very considerably, whereas those to France remained about the same; exports to the United States rose very little, and exports to Britain actually fell. The year-to-year growth in visible and invisible exports together should work out in terms of value at somewhere around 10 ½ %.

Neither the dampening effects of the revaluation nor the restrictive economic policy pursued proved capable of containing the highly expansionary movement of domestic demand quickly enough.

Enterprises' capital expenditure, particularly in the first half of the year, contributed strongly to exaggerating the boom. Despite the decidedly adverse trend in profits and costs, and the tighter credit policy making outside capital



harder to obtain and more expensive, enterprises went on stepping up investment, since sales prospects appeared to indicate that the excess demand was all set to continue. The consequent price increases, however, detracted from the results for the economy as a whole, as is evident from the 1970 investment figures. Thus, while investment in plant and machinery went up by an estimated 23% in money terms, the increase in real terms was probably more like 15%. However, these overall figures do not reveal a pattern of investment activity which became more and more differentiated as the year went on, with the propensity to invest becoming progressively cooler in consequence of the slowdown in orders and the additional restrictive measures introduced by the Government in the middle of the year.

In building investment the gap between the levels in terms of money and in real terms was wider still. The first half of the year saw a veritable price explosion, due in part to wage price increases, the incidence of which is high in the building industry. Production losses caused by weather conditions in the first quarter were also a contributing factor. Over the year as a whole, the increase in building investment was about 21.5 % in terms of value, but the real expansion, if the influence of the higher prices is subtracted, was probably no more than 4 ½ %. The price upsurge, which affected all departments of building more or less equally, hit residential building particularly hard: turnover here scarcely moved up at all from the spring onwards. But real growth of public investment—a major part of which is in building—was also appreciably eroded in 1970 by the rise in prices.

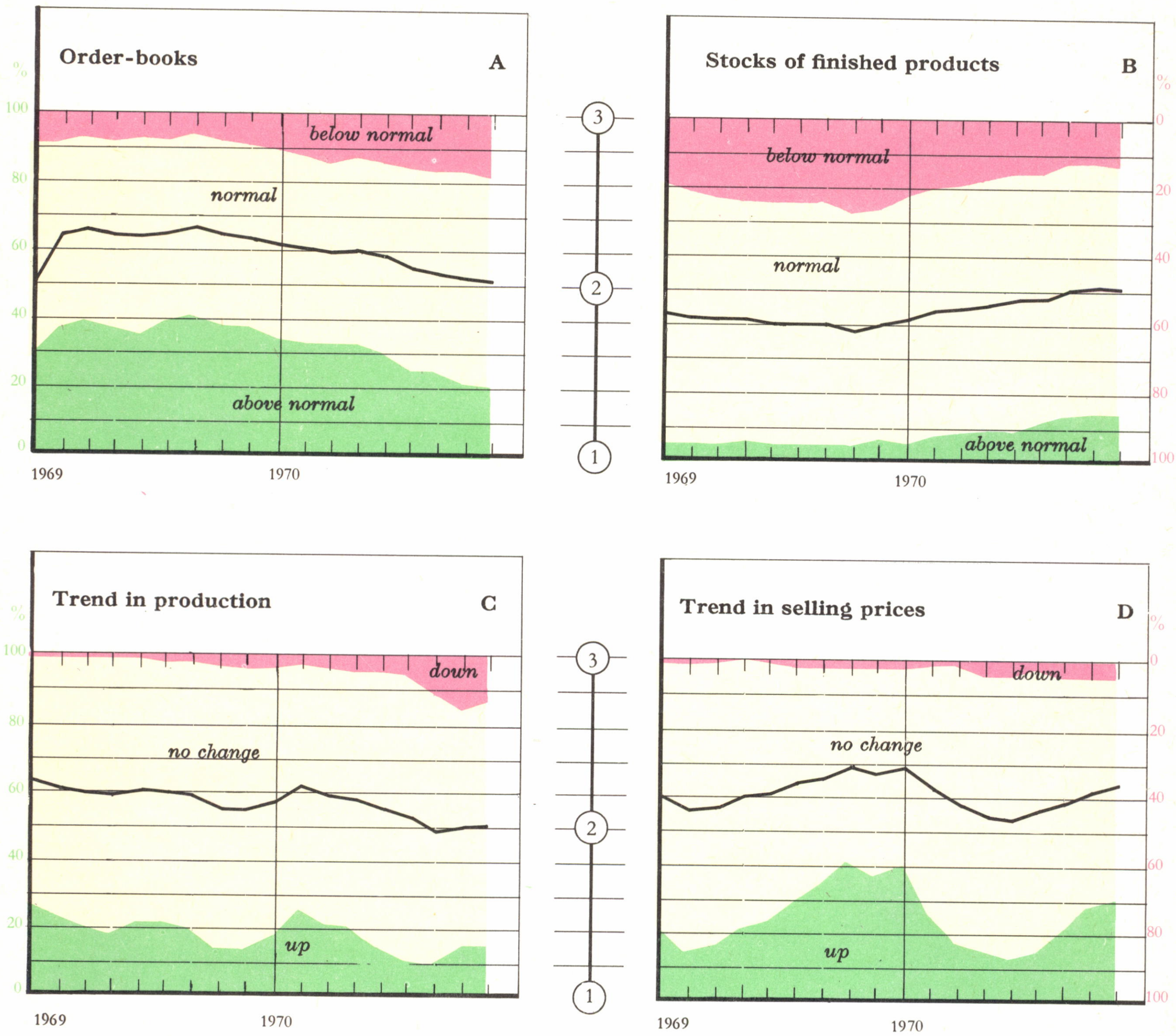
Stockbuilding on the other hand ceased, by and large, to provide any additional expansionary stimuli: on the contrary, the trend here helped to ease matters in some industries. The steel manufacturers and steel dealers in particular showed a tendency to call a halt in building up their stocks, and orders to the iron and steel industry accordingly went down. Judging by the relatively low imports of other important raw materials and semi-finished products, much the same is happening elsewhere, though not to such a marked extent. Even the retail trade, according to the EEC Business Survey, regarded the stock position as generally normal: despite the very brisk consumer demand, there was, if anything, some hesitation in placing new orders.

Public consumers' expenditure rose sharply in 1970, primarily in consequence of the increased wages and salaries payable from the beginning of the year.

In addition to the continued hectic investment activity in the early months, a steep climb in private consumers' expenditure in all branches manifested itself during 1970. The German consumer goods industries did not in fact do as well out of this boom as had been expected, owing partly to traders' cautious policy on stocks and partly to the pressure of supply of goods from abroad. Imports of consumer goods, notably motor vehicles and electrical appliances, went up very markedly. A further point was that quite a sizable portion of households' disposable income went on foreign travel: German tourists abroad in the holiday months of June, July and August spent about a quarter as much again as a year before. Notwithstanding, retail trade turnover in the first nine months was 11 % up on the first nine months of 1969. All in all, private consumers' expenditure, as defined for the national accounts, may be reckoned to have risen by 12 %, 4% of which would be due to price increases.

As regards incomes, 1970 was marked by a large wage and salary increases, and by a shift in the incomes pattern in favour of the workers.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Answers to questions in the EEC business survey, carried out in the German Federal Republic by the IFO-Institut.

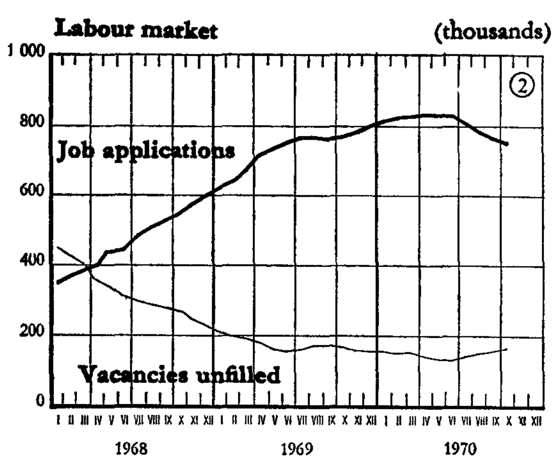
GRAPHS A, B, C and D : The three colours (green, yellow and red) show the percentages of the three different answers.

The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows :

by 0.03 for the answer "above normal", or "up";
by 0.02 for the answer "normal", or "no change";
by 0.01 for the answer "below normal", or "down".

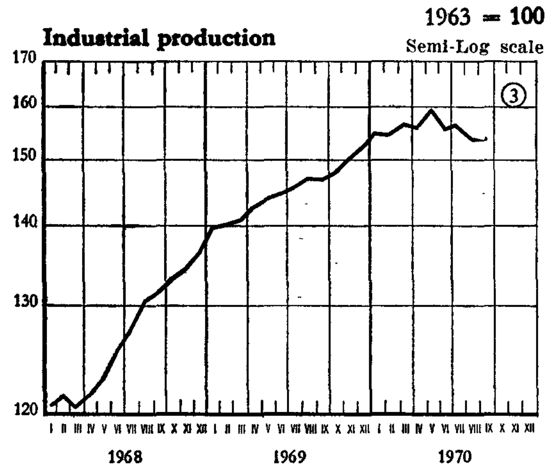
Collectively agreed wages were put up once again, but the wage pressure was also in part due to the granting of substantial extra amounts beyond the agreed rates. Altogether the gross wage and salary bill (including pay continued during illness, as required by a recent new law) probably increased by some 17 ½ %. Part of the increase in earnings was absorbed by the progressive tax scale, and part also, in the later part of the year, by the 10 % counter-cyclical income tax surchage introduced by the Government in the summer for the period August 1970-July 1971. Drawings of self-employed persons and unearned income increased only moderately, as also did transfer incomes, chiefly because pensions are calculated from the earnings of employed persons over the previous three years. One of the factors making for higher private consumer spending was a falling-off in the propensity to save : the proportion of incomes saved showed a definite drop, and the marginal savings ratio was actually negative.

Strains on the labour market owing to over employment became more acute than ever in the early part of the year. The general imbalance would certainly have hindered production even more than it did had not further large numbers of foreign workers been recruited. By the end of September close on two million non-German wage earners were employed in Germany—8.5% of all persons in paid employment and 450 000 more than in September 1969. This reflects the greater mobility of manpower resulting from economic integration,



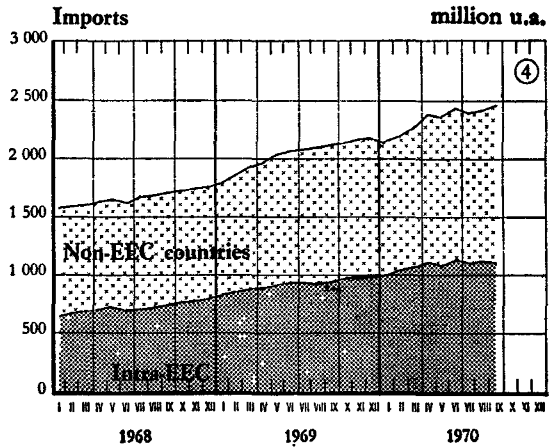
and also insufficient switching of investment flows into other regions of Europe with development potentialities. The average number of unemployed over the year fell to the practically irreducible level of 150 000, or 0.7 % of the total number of persons in paid employment. Conversely, the number of unfilled vacancies climbed to an estimated 820 000. The position tended to ease somewhat after mid-1970, but the tightness earlier on had been so great that overemployment still prevailed at the end of the year.

With overall demand soaring and bottlenecks increasingly obstructing efforts to expand capacity faster, the elasticity of domestic production became smaller and smaller as the year went on. Industrial production did show a 6 ½ % increase for the year as a whole, but much of the increase occurred right at the beginning; in fact, production even tended to dip slightly from the summer onward, mainly, it would seem, because of supply difficulties, but also, in some industries, because of customers' caution in stock policy and stiffer foreign competition.



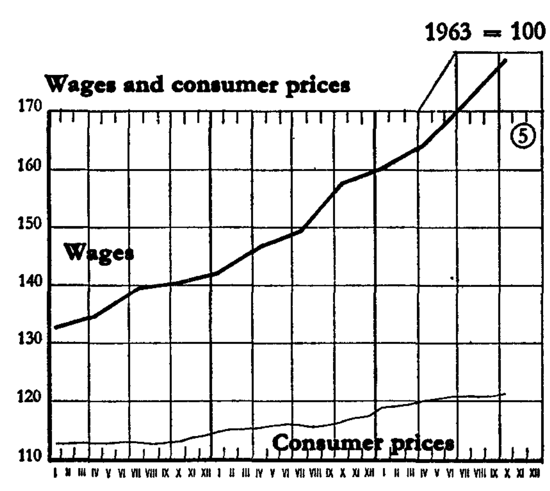
Generally speaking, production trends began to differ more from industry to industry. The increase in productivity in 1970 for all industries together was only about 3 %, compared with 7.5 % in the previous year. Of the other production sectors, agriculture yielded no more than an average harvest, while on the services side prices rose sharply and real expansion was slightly less than in 1969. Overall, the year-to-year growth in real gross national product may be put at 5 ½ %.

Taking the economy as a whole, less than had been expected was done in 1970 to relieve the pressure on domestic supply potential by stepping up imports. Decisive factors here were disinclination to add to stocks, which damped down imports of raw materials, and smaller imports of foodstuffs. Import demand in the overheated sectors, however, was very high—notably for capital goods, and also for consumer



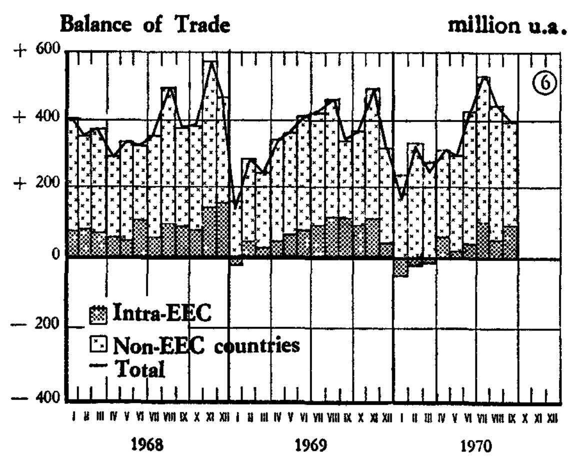
durables, foreign suppliers of which were increasingly active in exploiting the still better sales field afforded them by the revaluation. Visible imports according to the national accounts classification could have risen 13 % in value overall, and visibles and invisibles together by perhaps 13 ½ %.

The persisting demand/supply strains and the steep rise in wage costs brought a decided turn for the worse in the price position. Producer prices in particular went up faster in 1970 than ever before, those for industrial products standing in October 5.5 % above the previous Octo-

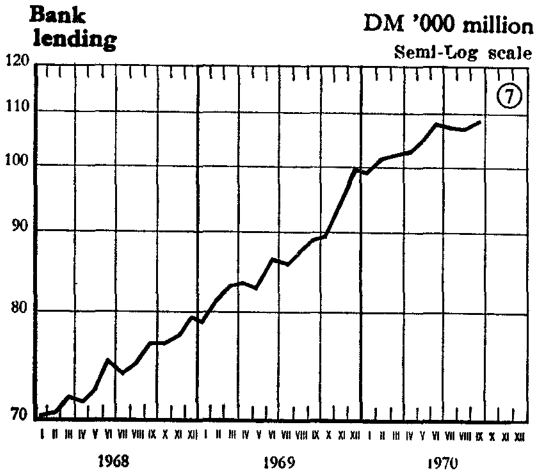


ber's level. This in turn sent up consumer prices, which at the same date were 4.0 % up on the previous October—5%, in fact, if we exclude foodstuffs, beverages and tobacco.

In terms of the trend the country's external trade surpluses decreased during 1970 : although the balance of visible trade for the first nine months closed with a surplus of DM 10 600 million, compared with DM 10 700 million for the first nine months of 1969, the deficit on service transactions more than trebled, to DM 3 100 million, and since in addition there was a considerable increase in transfer payments—chiefly by reason of larger remittances by foreign workers to their home countries—the surplus on current account for these nine months was down to DM 800 million, as against DM 4 100 million for January-September 1969. The trend in the long-term capital flow went into reverse. Net exports of long-term capital in the first three quarters totalled only DM 4 800 million—compared with DM 13 400 million in 1969, the year of the revaluation—and of this DM 4 000 million left the country during the first quarter. Largely on account of the restrictive policy, much greater recourse was had to short-term capital from abroad. The net inflow of such funds in the first three quarters am-



ounted to DM 9 200 million (as against DM 5 200 million in 1969), enterprises' borrowings accounting for DM 5 500 million; the substantial credit balance on statistically unclassifiable transactions—mainly represented by changes in leads and lags—likewise reflects large incomings of short-term capital. The consolidated foreign exchange holdings of the Bundesbank and the commercial banks were up by DM 11 100 million net by September, the Bundesbank's currency reserves at end September standing at approximately DM 41 400 million, in contrast to the low level of DM 26 400 million touched at end December 1969.



Monetary expansion accelerated during 1970 : the money supply[1] rose in the first nine months by DM 6 100 million—whereas in the first nine months of 1969 it had fallen by DM 300 million —and in September was 17 % above the figure for the previous September. This was due principally to the large increase in the Bundesbank's net claims on foreign debtors as a result of capital imports by enterprises, and to the further extension of credit, which continued in full swing; lending to firms and individuals was up 7.5 % and to public authorities up 5 % in the first nine months.

[1] Notes and coin outside the credit institutions, together with sight deposits and time deposits at less than three months' notice.

Demand for and supply of goods and services

	1968 [1]	1969 [1]		1970 [2]		1971 [3]
	At current prices (in DM '000 million)	% change on preceding year				
		Volume [5]	Value	Volume [6]	Value	Volume [6]
Exports [4]	124.4	+ 11.9	+ 13.8	+ 7½	+ 10½	+ 6½
Gross fixed asset formation	124.8	+ 12.1	+ 17.2	+ 9	+ 22	+ 5
Public current expenditure on goods and services	83.6	+ 4.3	+ 12.1	+ 2½	+ 12	+ 4½
Private consumers' expenditure	301.1	+ 8.0	+ 10.8	+ 8	+ 12	+ 4½
Gross national product	538.5	+ 8.0	+ 11.8	+ 5½	+ 13	+ 3½
Imports [4]	106.4	+ 16.2	+ 18.8	+ 14	+ 13½	+ 8½

[1] Federal Statistical Office, «Wirtschaft und Statistik», No. 9/1970.
[2] Commission estimates.
[3] Commission forecasts.
[4] Goods, services and factor income.
[5] At 1962 prices.
[6] At preceding year's prices.

Note :

(*a*) The difference between the figures for demand and those for supply is accounted for by movements in stocks.
(*b*) The forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with the experts of the member countries but are established and published on the sole responsibility of the Commission.

In addition, the formation of monetary capital at the banks did not offset monetary expansion to the same extent as in 1969, by reason of smaller in-payments on longer-term time and savings deposits. The bank liquidity position reflected the inflow of liquidity from abroad during the year : after tightening markedly in the first quarter, the liquidity ratio thereafter rose again.

The cash transactions of the public authorities again had a restrictive effect on bank liquidity in the first three months, partly owing to the action of the Federal and Land authorities in placing a counter-cyclical equalization fund of DM 3 000 million in the Bundesbank. Expenditure increased more or less as provided for during the first nine months, but appears to have gathered pace after that. Another factor in the worsening of the cash positions was the comparatively small rise in revenue from the assessed income tax and company tax; on the other hand, the counter-cyclical surcharge payable from August on, which does not figure in the budgets, took some DM 2 400 million out the domestic economy.

In the capital markets, the effect of the restrictive monetary policy was to send interest rates up strongly, so that for a time they were well above those ruling abroad and attracted capital inflows which ran counter to the policy. The average yield from bonds was up by June to 8.8 %, higher than at any time since the war. A slight temporary downturn in interest rates did occur, however, after the middle of the year, when international rates began to fall again and the Bundesbank, following the Government's additional stabilization measures, concentrated its restrictive action more on the liquidity side, by lowering Bank rate from 7 ½ % to 7 %.

2. Outlook for 1971

Three distinct and to some extent conflicting trends are discernible in the picture for the beginning of 1971 : on the one hand investment demand and the flow of orders from abroad are definitely settling towards a more normal level, while on the other wages are going up well beyond any possibility of productivity gains to match, and the resulting consumption boom appears likely to continue. While the return to normal in some demand sectors is most welcome, and is in fact one of the aims of short-term economic policy, it will be particularly unfortunate if the steep climb in wage costs persists inasmuch as it may cause enterprises' investment activity to flag appreciably as the year goes on.

How far foreign demand will be covered may depend in considerable measure on what further easing occurs in domestic demand and to what extent enterprises respond by exporting more. So far as demand is concerned at all events, as is shown in detail elsewhere in this Survey, world trade seems all set to undergo further vigorous expansion. The American business revival, in particular, will offer increased outlets for German exports. In Europe, on the other hand, with the demand inflation progressively lessening, international competition and the effects of the 1969 parity changes and of the cost upsurge in Germany will be more in evidence. The growth in exports overall will probably be about the same as in gross national product in money terms.

Along with consumers' expenditure, the main influence on the movement of business will be capital expenditure. Much will depend, in particular, on how the enterprises react in their investment planning to yet more rapidly rising costs and narrower profit margins. For the purposes of the 1971 forecasts it has been assumed that enterprises have two courses open to them for trying to contain their costs : they can cut their capacity utilization to the level that is most advantageous costwise, or they can go ahead with their structural investment projects in order to have more and better potential available to meet the expected upturn later on.

Then again, it is hard to say at present to what extent firms which have delayed placing orders for capital goods while depreciation by the decreasing-line method was in abeyance, until the end of January, will make up for lost time after that. The Commission expects that investment in 1971 will rise decidedly more slowly, without actually going into recession; with a very heavy backlog of orders still in hand at the beginning of the year, and capacity utilization by no means very markedly down as yet, there are good prospects of its setting gently to a normal level. The IFO Institute's November 1970 survey of EEC investment does not suggest excessive decline in the propensity to invest, since it records that firms are still planning to step up their investment expenditure by 8 % in 1971. As regards investment in building, industrial building, to judge by the licences issued, is set to continue very actively for some time to come. Residential building will remain under strain, with demand tending to grow too fast and supply not fast enough. On the public works side, expansion in terms of money will certainly be considerably greater than in 1970.

Any braking effect from investment in stocks will probably be on a smaller scale this time than in the later stages of previous business cycles, especially as in many industries the adjustment of stock levels to the change in the sales prospects has already been made, in 1970. As regards consumer goods, in fact, stock-building could touch off a further upturn, if anything.

The rise in consumer spending by households during 1971, though probably somewhat less lively than before, can be expected to remain a major factor for buoyancy. The wage and salary awards since the autumn of 1970 alone should cause incomes to increase substantially again, and it is doubtful whether the upward movement of wages in 1971 will return before too long to proportions which the economy can reasonably accommodate. Transfer incomes, it is true, should rise to only the same moderate extent as in 1970 and, with profits shrinking, withdrawals from businesses should, as before show a comparatively small increase. Also, the larger amounts deducted in tax in 1971 should notably hinder the upswing in consumption. Quite apart from the normal fact of higher earnings being taxed higher under the progressive scale, a sizeable part of the increase will also be absorbed by the counter-cyclical surchage of 10 % imposed until the summer of 1971 for the purpose of curbing consumption. This can be expected during 1971 to neutralize something like DM 2 500 million or more of purchasing power—about 7 % of the estimated increment in incomes. Finally, a further decline in households' propensity to save is hardly likely in 1971.

The easing of overall demand should scarcely be marked enough, in the first half-year at any rate, to bring the relationship between supply and demand really back into balance. After years of overstrain of the available potential, the elasticity of supply has for some time been low. The potential will, admittedly, be enlarged as a result of the substantial investment in extra capacity during the last few years. It looks, however, from the current slowdown—already very much in evidence towards the end of 1970 —as if the 1971 growth rate in industrial production will be rather below the trend charted for the medium term. The shares of the other sectors, and especially of services, in gross national product will show a further increase. Altogether, given the present cyclical trends, the increase in real gross national product from 1970 to 1971 should work out at round 3 ½ %.

Under these conditions, a cyclical slowdown in the growth of imports would appear to be highly feasible. For imports of raw materials will probably increase only to the extent needed to cover additional production requirements, and the hitherto rocketing imports of consumer durables may well lose momentum, partly from the movement of demand and partly also from intensified sales drives by German enterprises. Nevertheless, in 1971 the balance of exports less imports will probably once again account for a slightly smaller proportion of gross national product than before.

Everything indicates that the general price level will go up rather less from 1970 to 1971 than from 1969 to 1970. Nevertheless, the consumer price situation will remain exceedingly precarious and could very easily take a temporary turn for the worse, particularly in the first half of the year. This will be especially liable to happen if enterprises, instead of playing along with the boom and seeking to work up their sales—which would in itself be a good thing do do at this stage in the cycle—succumb to the temptation of yet again passing a large part of their cost increases on to prices. By so doing they would impede if not halt the gradual return to more normal conditions which has now set in, and run the risk of incurring a correspondingly sharper downturn later.

In their short-term economic policy during 1970 the Bundesbank and the Federal Government adopted an increasingly restrictive line in order to reduce the overheating that was developing, and they should continue to rely principally on the same weapons—monetary restrictions and the tax measures introduced in mid-1970—in the months ahead. At this juncture, with calmer conditions in sight and the boom showing signs of tapering off in some sectors, there is grave danger of the business climate's deteriorating in consequence of a sharp leap in the wage-price spiral. Only by carefully steering the economy back into calmer waters will it be possible gradually to even out the imbalances that have appeared in the last two years and so restore stability, as required by the Community's draft third Medium-term Economic Policy Programme. This would indeed involve letting growth dip slightly below the rate charted for the medium term, for a while, but would reduce the risk of a turnround into recession.

A great deal hinges on the attitude of the two sides of industry. Wage and price increases higher than the economy can properly afford could have implications for the whole short-term economic policy. If the employers and workers persist on an inflationary course when the excess demand is in fact abating, there might even be no alternative but to tighten the squeeze still further. To obviate this, managements should make a point of looking well ahead, and meanwhile exercise moderation in pricing so as to take as much advantage as possible of the present quantity boom. The workers for their part should make more allowance for business conditions in the scaling and timing of their wage claims; this will not, after all, after the distribution of incomes to their detriment. The Government has indicated, as a guide for the impeding collective bargaining agreements, that a 7-8 % increase in actual earnings would be economically acceptable—a figure well below the levels fixed in the most recent settlements.

This approach, which was adumbrated in the Community's stabilization programme, will involve keeping public spending within the most stringent limits during the first half of the year. The Federal budget before the Bundestag provides for an increase in expediture by a good 12 %, and the draft Land budgets about the same—over three times the amount of the expected growth of real gross national product. The actual spending should be so managed in the first six months as to keep the rate of increase well below that estimated for the year as a whole, notably by means of a temporary freeze on certain items. Orders should be timed and distributed so as to be carried out, as far as possible, mainly in the second half of the year, when conditions are expected to be less strained. As regards revenue, efforts should be made to speed up the collection of income tax, which fell far behind schedule in 1970.

Monetary and credit policy, which bore the main burden of the restrictive measures of the first half of 1970, may be hampered even more in 1971 by the effects of the balance of payments. If the large inflows of liquidity continue, monetary policy may have to be remodelled yet again, in the first place to iron out the differences between German and foreign interest rates[1]—though as a matter of fact these capital movements are not due entirely to the interest differential, but also in part to the strained financing position of German firms.

Major economic policy measures

June

(1) On 4 June, the Bundestag passed the third law on the promotion of private capital formation, which makes the following notable changes. The tax exemption ceiling for asset-creating benefits is raised from DM 324 to DM 624 p. a., with retrospective effect from 1 January 1970. From 1 January 1971, in place of the previous exemption of savings from tax and social security contributions, a state savings supplement of 30 % of the amounts invested (or 40 % for persons in paid employment with three or more children) is to be granted provided the taxable income does not exceed DM 24 000 in the case of single and DM 48 000 in the case of married persons.

(2) On 18 June, the Bundestag voted the Federal budget for 1970, which totalled

[1] The Bundesbank took steps along these lines on 17 November 1970, after the present Survey had been completed. The discount rate was lowered from 7 to 6 ½ % and the rate for advances on securities from 9 to 8 %. At the same time the minimum reserve ratio for additions to domestic liabilities was abolished with effect from 1 December 1970, and instead the minimum reserve ratio for all bank liabilities was raised by 15 %. The overall result is a slight further reduction in bank liquidity.

DM 90 950 million. This includes DM 1 500 million to be immobilized by the Federal Government in the Bundesbank as a counter-cyclical equalization fund. In addition, expenditures to a total of DM 440 million were blocked. After deduction of these amounts, the 1970 budget works out 9 % above the actual expenditure for 1969.

July

(1) On 1 July, the Bundesbank made an across-the-board increase of 15 % in the minimum reserve ratios, to take effect forthwith. This was done in order to offset in part the effect which the inflow of capital from abroad has been having on liquidity.

(2) On 6-7 July, the Federal Government adopted an economic stabilization programme, comprising the following measures :

(a) To curb investment activity, diminishing-balance depreciation on movable assets and the system of higher depreciation allowances on fixed assets represented by buildings (except dwellings) were placed in abeyance until 31 January 1971. The consequent shift in investment could amount to some DM 3-4 000 million.

(b) A temporary surcharge of 10 % was imposed on income, payroll and corporation tax falling due between 1 August 1970 and 30 June 1971 (with exemption for taxpayers liable for only DM 100 a month or less), to be refunded by not later than 31 March 1973. The Federal Government has the right to reduce the rate of surcharge, to shorten the period during which it is levied, and to advance the date of refund.

These measures were approved by the Bundestag on 11 July and by the Bundesrat on 15 July.

(c) All the restraint the economic policy demands is to be observed in drawing on the Federal appropriations for 1970; expenditures deferred up to now are not to be effected all at once.

(d) Projected tax concessions (the raising of the tax-free allowance for wage and salary incomes to twice its previous level, the scaling-down of supplementary charges) are to be held over to a date considered suitable under terms of the economic policy.

(3) On 9 July, the Government adopted the Federal budget estimates for 1971, and the revision and elaboration of the medium-term finance plan to cover the years 1970-74. The 1971 estimates provide for a total expenditure of approximately DM 100 100 million, 12.5 % above the corresponding figure for 1970 (less the counter-cyclical equalization reserve of DM 1 600 million). Net borrowings come out at DM 2 900 million. The implementation of the budget is to be further reviewed early in the new year in the light of economic developments. The medium-term finance plan allows for rises in Federal expenditure of 8.5 % in 1972, 8.25 % in 1973 and 8.0 % in 1974.

(4) The Bundesbank lowered the discount rate from 7.5 to 7 % and the rate for advances on securities from 9.5 to 9 % with effect from 16 July.

August

On 12 August, the Bundesbank decided on a stepped increase in minimum reserves : from 1 September 1970, additions to credit institutions' reserve-carrying liabilities in respect of sight and time deposits will be subject to an additional minimum reserve ratio of 40 % (savings deposits 20 %). At the same time the additional reserve ratio for deposits by customers abroad was abolished.

October

On 22 October, the Federal Government adopted "target figures for general economic development in 1971". For coming wage agreements, a target is suggested of 7-8 % increases in actual earnings. At the same time the Government expects enterprises, with an eye to the longer-term trend of the market, to take relatively little advantage of such scope as they still have for passing cost increases on to prices, and accept smaller profit margins for the time being. Should the trend of the economy in 1971 show signs of diverging widely from that which these guidelines are intended to encourage, the Government will in due course consider taking further steps to assist the restoration of normal conditions.

Germany

TABLE 1 : **Key indicators**

	1965	1966	1967	1968	1969	1969
	% change by volume on preceding year					1963=100
Gross national product	5.6	2.9	– 0.3	7.2	8.0	134
Industrial production	7.3	2.5	– 2.4	9.5	10.4	141
Total imports	14.2	2.6	– 1.3	14.7	16.2	172
Private consumers' expenditure	6.7	3.7	0.6	4.0	8.0	131
Public current expenditure on goods and services	4.8	2.1	3.3	– 0.9	4.3	114
Gross fixed asset formation	4.6	0.9	– 8.4	8.0	12.1	131
Total exports	7.5	10.7	8.5	13.4	11.9	181
Gross national product per head of population	4.3	1.8	– 0.7	6.6	6.6	127
Gross national product per person in employment	4.9	3.2	2.7	2.7	6.1	134
	% change by value on preceding year					
Gross income per employee	8.9	7.5	3.4	6.5	9.6	153

TABLE 2 : **Indicators for internal and external equilibrium**

	1965	1966	1967	1968	1969
Balance exports less imports					
in million u.a.	– 135	+ 1 613	+ 4 063	+ 4 063	+ 3 906
as percentage of GNP	– 0.1	1.3	3.3	3.3	2.5
Unemployment rate	0.5	0.6	1.7	1.2	0.7
prices to private consumers (% change on preceding year)	+ 3.2	+ 3.5	+ 1.7	+ 1.8	+ 2.5

TABLE 3 : Foreign trade (at current prices)

	% change on preceding year					1963=100	Million u.a.	% of totals
	1965	1966	1967	1968	1969	1969	1969	1969
Visible exports								
Total	10.3	12.5	8.0	14.3	16.9	199	29 053	100.0
Intra-EEC	6.7	16.0	9.4	16.7	23.9	212	11 571	39.8
To non-EEC countries	12.4	10.6	7.2	12.9	12.8	191	17 481	60.2
Exports of food, beverages and tobacco								
Total	25.0	− 2.0	26.9	21.8	27.0	290	836	2.9
Intra-EEC	22.6	6.6	61.2	32.8	31.0	447	496	1.7
To non-EEC countries	26.6	− 7.3	2.6	9.4	21.6	191	340	1.2
Exports of raw materials, fuel and power								
Total	3.4	7.1	1.3	10.7	4.2	131	1 635	5.6
Intra-EEC	4.1	8.5	1.5	10.6	5.4	132	1 009	3.5
To non-EEC countries	2.3	5.0	0.4	11.5	2.4	129	627	2.1
Exports of semi-finished and finished industrial goods								
Total	10.1	13.8	6.6	15.9	17.5	203	26 581	91.5
Intra-EEC	5.3	18.9	4.7	21.6	25.8	220	10 066	34.6
To non-EEC countries	12.7	11.3	7.6	13.0	13.0	194	16 515	56.9
Visible imports								
Total	19.6	3.2	− 3.7	16.1	23.7	192	24 933	100.0
Intra-EEC	30.7	4.2	− 1.0	21.7	30.0	250	10 862	43.6
From non-EEC countries	13.6	2.5	− 5.4	12.5	19.3	162	14 071	56.4
Imports of food, beverages and tobacco								
Total	21.6	2.4	− 4.2	3.7	16.7	156	4 333	17.4
Intra-EEC	28.0	6.8	0.1	11.9	26.8	212	2 045	8.2
From non-EEC countries	18.1	− 0.1	− 6.9	− 1.9	9.0	127	2 288	9.2
Imports of raw materials, fuel and power								
Total	4.6	2.8	− 0.6	15.8	12.2	162	5 825	23.3
Intra-EEC	8.3	8.1	9.4	18.1	23.3	218	1 195	4.8
From non-EEC countries	3.9	1.8	− 2.5	15.3	9.7	152	4 630	18.5
Imports of semi-finished and finished industrial goods								
Total	27.2	3.6	− 5.0	21.1	31.4	222	14 775	59.3
Intra-EEC	35.7	2.8	− 3.0	25.4	32.0	270	7 623	30.6
From non-EEC countries	20.0	4.3	− 6.9	16.8	30.7	187	7 153	28.7

TABLE 4 : Selected monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production	1968	118.3	119.7	123.7	122.1	123.8	131.5	126.3	135.7	133.0	131.2	139.7	139.6
(1963 = 100)	1969	138.9	141.4	143.5	142.2	146.1	146.2	144.5	150.3	145.8	147.6	157.8	153.9
	1970	155.0	156.8	159.7	152.8	164.9	151.0	154.5	157.7	151.1			
New orders received	1968	128.2	132.3	127.0	135.2	145.5	127.4	140.9	143.2	143.9	155.0	149.7	147.8
(1963 = 100)	1969	163.0	161.6	166.2	169.3	168.0	166.1	176.6	174.8	177.6	179.6	172.0	170.9
	1970	176.6	185.3	179.5	184.3	169.0	182.3	178.5	176.0	176.0			
Unemployed	1968	460.0	378.5	387.8	331.9	313.1	301.7	287.0	287.1	264.7	252.3	235.7	209.4
(1 000)	1969	197.0	203.3	185.0	156.0	162.3	171.5	178.4	177.1	166.0	161.3	148.3	150.6
	1970	162.1	142.3	156.1	121.1	132.9	140.5	151.6	157.1	159.8	162.0		
Construction : permits for	1968	43.3	48.5	49.7	47.7	43.9	40.7	42.4	45.3	45.5	43.6	42.6	44.0
residential construction	1969	43.4	47.2	44.8	45.6	47.2	48.1	48.4	45.6	47.0	49.3	48.7	44.2
(1 000)	1970	49.0	50.7	46.0	52.6	47.4	51.6	55.4	54.5	54.5			
Private consumers' expen-	1968	150.2	152.9	148.9	158.5	155.1	152.1	158.7	162.1	157.5	159.5	167.9	156.1
diture : department store	1969	164.1	155.7	162.3	159.4	170.6	167.7	170.1	172.3	175.9	180.7	179.3	181.0
turnover (1963 = 100)	1970	185.3	176.4	185.6	180.7	185.6	198.1	202.8	189.8	195.0			
Consumer prices	1968	112.8	112.8	112.9	112.9	112.9	113.1	113.1	112.8	112.9	112.3	113.9	114.3
(1963 = 100)	1969	115.1	115.4	115.5	115.7	115.9	116.2	116.1	115.8	116.1	116.5	117.0	117.6
	1970	119.1	119.3	119.8	120.1	120.3	120.7	120.7	120.6	120.6	121.2		
Visible imports	1968	1 530	1 618	1 606	1 638	1 686	1 504	1 829	1 686	1 674	1 833	1 732	1 694
(million u.a.)	1969	1 933	1 880	1 973	2 071	2 021	2 043	2 144	2 041	2 122	2 393	2 124	2 124
	1970	2 338	2 482	2 377	2 631	2 351	2 608	2 538	2 380	2 508	2 475		
Visible exports	1968	1 930	1 965	1 979	1 922	2 011	1 818	2 181	2 181	2 053	2 215	2 305	2 171
(million u.a.)	1969	2 069	2 156	2 217	2 402	2 380	2 446	2 559	2 480	2 457	2 785	2 616	2 469
	1970	2 507	2 785	2 634	2 935	2 650	3 028	3 083	2 822	2 873	2 932		
Balance of trade	1968	+ 400	+ 348	+ 373	+ 284	+ 325	+ 314	+ 352	+ 495	+ 379	+ 382	+ 573	+ 477
(million u.a.)	1969	+ 137	+ 276	+ 244	+ 331	+ 359	+ 404	+ 415	+ 439	+ 335	+ 392	+ 492	+ 345
	1970	+ 168	+ 304	+ 257	+ 304	+ 299	+ 420	+ 545	+ 442	+ 365	+ 457		
Official gold and foreign	1968	6 486	6 749	7 030	6 842	6 732	6 733	6 721	6 695	6 962	6 665	8 543	7 497
exchange reserves	1969	6 229	6 169	5 926	6 473	9 326	7 738	7 762	8 322	9 664	8 165	6 889	5 679
(million u.a.)	1970	5 951	6 112	6 241	6 354	6 633	7 594	8 538	8 740	9 762	10 339		
Money supply	1968	83.4	82.8	83.3	83.3	83.9	84.8	84.9	85.7	86.8	86.3	87.5	88.3
(DM '000 million)	1969	89.2	89.2	90.7	90.3	91.5	92.2	94.3	92.2	94.3	93.7	95.0	93.2
	1970	96.1	95.9	97.5	96.6	97.1	97.8	99.7	99.5	99.2			

Germany

NOTES TO GRAPHS AND TABLES

Source: Statistical Office of the European Communities (except as otherwise indicated).
Conversion into units of account (1 u.a. = 0.888671 g of fine gold = US $ 1) at official exchange rates.

Graph 1

— Exports (fob) : series adjusted for seasonal variations; three-month moving averages.

Graph 2

— Labour market: series adjusted for seasonal variations; three-month moving averages; position at end of month.

Graph 3

— Industrial production : excluding construction, food, beverages and tobacco; adjusted for seasonal variations; three-month moving averages.

Graph 4

— Imports (cif) : series adjusted for seasonal variations; three-month moving averages.

Graph 5

— Wages and consumer prices: index of average hourly gross earnings in industry (including construction); cost-of-living index (all households) at middle of month, not adjusted for seasonal variations.

Graph 6

— Balance of trade : difference between values of exports and imports seasonally adjusted.

Graph 7

— Bank lending: short-term loans to business and private customers within the country; position at end of month, not adjusted for seasonal variations.

Table 1

— Gross national product at market prices.
— Industrial production: value added by industry (including small workshops).
— Total exports and imports: goods, services and factor income.
— Gross income per employee: income from paid employment (including employers' share of social insurance contributions).

Table 2

— Balance exports less imports: as defined for the national accounts.
— Unemployment rate: number of unemployed as percentage of total labour force (annual averages); source: Statistisches Bundesamt and Bundesanstalt für Arbeit.
— Price index: price index of private consumption adjusted by the GNP deflator, computed from the national accounts.

Table 3

— Exports fob, imports cif. The products have been regrouped on the basis of the Statistical and Tariff Classification for International Trade (CST): food, beverages and tobacco (Groups 0 and 1 CST), raw materials, fuel and power (Groups 2-4 CST), semi-finished and finished industrial goods (Groups 5-9 CST).

Table 4

— Industrial production: adjusted for seasonal variations, excluding construction, food, beverages and tobacco.
— New orders received: manufacturing industry (excluding food, beverages and tobacco); seasonally adjusted value index.
— Unemployed: position at end of month, adjusted for seasonal variations.
— Construction: seasonally adjusted number of dwellings authorized.
— Private consumers' expenditure: seasonally adjusted value index of department store turnovers.
— Consumer prices: cost-of-living index (all households), not adjusted for seasonal variations.
— Imports cif, exports fob; value, adjusted for seasonal variations.
— Balance of trade: difference between values of imports and exports seasonally adjusted.
— Official gold and foreign exchange reserves: gross reserves of gold and convertible currency with Bundesbank at end of month.
— Money supply: notes and coin in circulation (excluding cash holdings of credit institutions) and sight deposits of domestic non-banks (excluding public authorities' deposits with the Bundesbank); seasonally adjusted end-of-month figures.

B. France

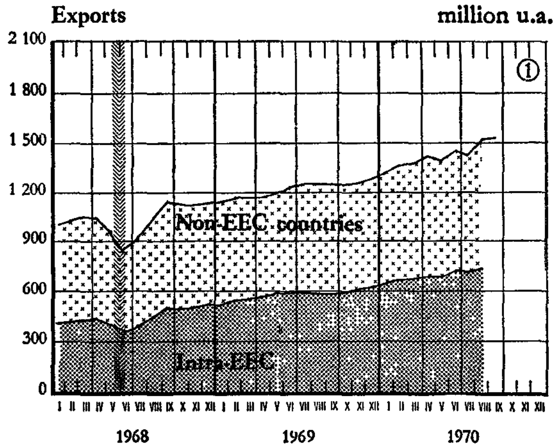
Rapid and very substantial progress was made towards the re-establishment of external equilibrium in 1970, thanks to the devaluation of August 1969 and the ensuing energetic implementation of the stabilization programme. The trade deficit shrank, a considerable surplus was again achieved on the balance of payments, and the persisting inflow of foreign currency made it possible to pay back short-term foreign debts promptly and rebuild foreign currency reserves. It proved more difficult to re-establish internal equilibrium in a world business situation which was very much affected by inflationary pressures. Households' greater propensity to save admittedly reduced tension on the consumer goods market to a telling extent; but the unexpectedly vigorous export upswing and the resulting further strengthening of the investment boom kept the level of utilization of production capacity and labour resources very high well into 1970. Costs and prices continued to rise sharply.

For these reasons, and also on employment policy grounds, short-term economic policy should continue to give priority to consolidating the basis for the fastest possible longer-term growth of the French economy in conjunction with greater stability at home and preservation of the country's international competitive position. The public authorities in particular should follow this line, more especially since everything points to a powerful recovery of private consumption, a continuing high level of investment by enterprises, and the persistence of autonomous upward pressures on wages and prices, while at the same time it may well become harder to sell more abroad.

1. Balance-sheet for 1970

Externally, the devaluation of the franc in August 1969 and the implementation of a comprehensive stabilization programme very quickly achieved their aims in 1970. The trade deficit contracted considerably, the balance of payments again showed large surpluses, and the net foreign exchange position greatly improved. It was found more difficult to get the economy back into equilibrium at home—a major impediment being the unexpectedly strong export boom. Money supply admittedly grew at a distinctly slower rate, and production strains eased gradually, but costs and prices continued to rise sharply.

Exports undoubtedly set the pace in 1970. They increased unusually rapidly, thanks to the damming-back of home demand and a very lively expansion of foreign demand under the stimulus of inflation. French exporters increased their share of nearly all major markets, even though they did not make much use of the opportunity offered them by the devaluation to lower their export prices expressed in dollars. Among the other EEC countries, demand was particularly great from Italy and Belgium, whereas sales in Germany advanced relatively slowly—at least in the first half of the year—despite the additional advantage of the revaluation of the mark. There was also an exceptionally sharp increase in exports to non-member countries—more especially to Great Britain and to the United States, despite the very sluggish trend of internal business activity in these two countries. All in all, visible exports probably went up by about 28 % in value during 1970 (at



export prices which, expressed in francs, were, on average, some 8.5 % higher than in 1969). Invisible exports will also have forged ahead; earnings from tourism, in particular, may well have increased faster after the devaluation.

This growth of exports determined the level of production and employment in 1970 in no small measure, directly but also, and above all, indirectly—by exerting a quite decisive influence on the trend of investment. The export-orientated industries were, in fact, induced by soaring turnovers and profits to make a particularly large increase in their expenditure on fixed investment—which was well over a third up on 1969 according to the results of the INSEE investment survey. It can be assumed that private industry as a whole invested about 26 % more, even though as late as November 1969 businessmen's plans for 1970 only pointed to an increase of barely 20 %. The sharp strengthening of the propensity to invest in the course of 1970 is all the more noteworthy since the monetary and credit policy remained very restrictive to begin with and was only relaxed to some extent after mid-year. It seems that not only were the possibilities of self-financing still very great but also that there were no insuperable obstacles to borrowing: the home capital market was extraordinarily liquid, capital held abroad could be repatriated, and medium- and long-term loans for capital investment purposes were available in not inconsiderable amounts from special credit institutions. Furthermore, the high level of interest rates clearly had no more than a marginal impact, owing to expectations of higher prices.

In the first half of the year, on the other hand, the investment activity of public enterprises and public authorities clearly reflected the efforts made to balance the budget and curb subsidies. Expenditure only seems to have started to climb more steeply in the closing months of the year, more particularly in the field of low-cost residental construction, after the release of additional resources from the economic action fund and the disappearance of certain administrative obstacles. Private residential construction, which initially reacted with a substantial reduction in the launching of new projects after the speculative excessive increase of 1969, may well have picked up later in the year as well, when mortgage loans were again granted more freely. All in all, expenditure on gross fixed asset formation will have increased hardly less from 1969 to 1970 than from 1968 to 1969.

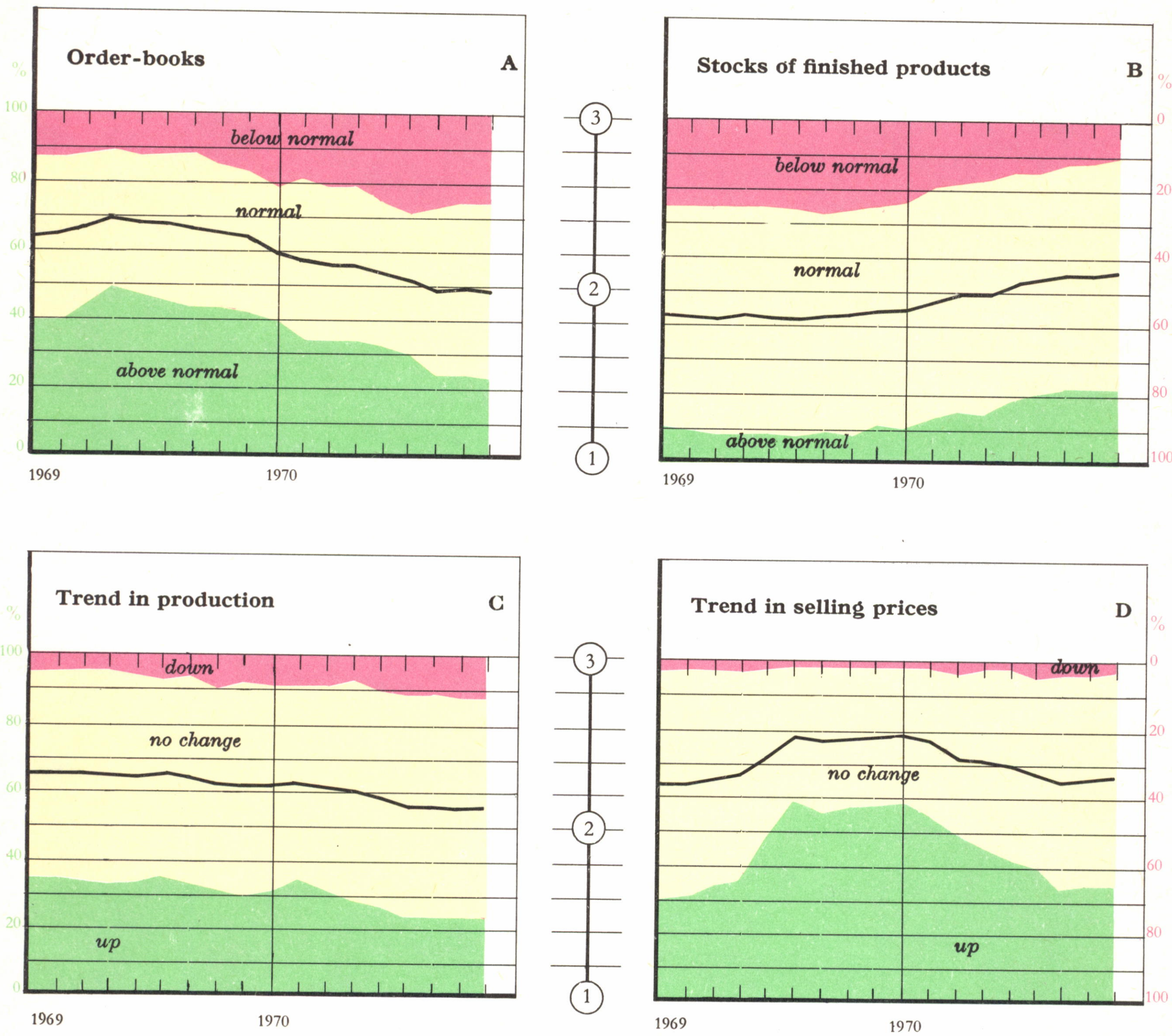
On balance, however, investment in stocks probably did not have such a strong impact in 1970 as in 1969. There was a further appreciable addition to stocks in the first half of the year, since the level—more especially of capital goods and certain primary products—was still considered below normal compared with turnover, but also because the trend of sales—particularly those of dealers and some industries near the consumer stage—failed to measure up to expectations. However, in the second half of the year, investment in stocks is likely to have lost momentum.

Consumption presented a decidedly quiet picture at times, compared with the buoyancy of exports and investment.

The annual rate of growth of public current expenditure on goods and services was hardly less high than from 1968 to 1969, but was affected in the early months of 1970 by restrictive budget management, which led to the postponement of certain purchases of goods and materials, while wage and salary payments rose fairly steadily and sharply in the course of the year.

Private consumers' expenditure in particular continued to exert a real inhibiting influence till well into the second quarter. Consumers put off further buying at first, in the aftermath of the "spending spree" of 1968/69 in which households had very rapidly stocked up with goods, especially consumer durables. They were further deterred by the tightening of consumer credit regulations and more generous in-

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Answers to questions in the EEC business survey, carried out in France by INSEE.

GRAPHS A, B, C and D : The three colours (green, yellow and red) show the percentages of the three different answers.

The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows :

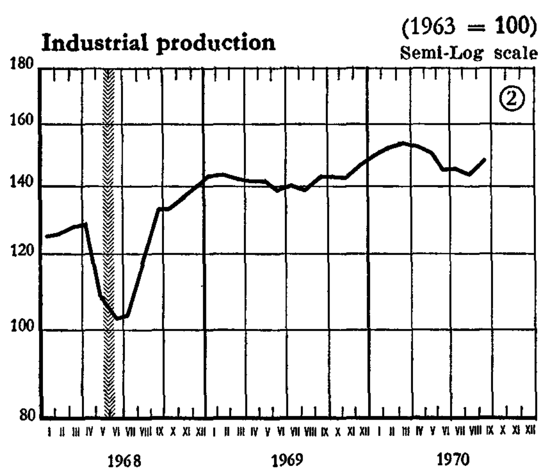
by 0.03 for the answer "above normal", or "up";
by 0.02 for the answer "normal", or "no change";
by 0.01 for the answer "below normal", or " down".

centives to save. New passenger car registrations and purchases of electrical domestic appliances and machines were well below the level for the previous year.

Some shift of expenditure to services probably occured, especially as the price rise here was particularly marked. However, there is no doubt that households increased their savings ratio appreciably in the early months of the year and only began to bring their consumer expenditure more back into line with the trend of their income in the summer. Private consumers' expenditure over the year as a whole may well have been about 10 ½ % higher than in 1969, although about 5 ½ % of this is attributable to the rise in prices.

The gross incomes of households would appear to have risen fairly steadily throughout the year, and the underlying trend was probably hardly less steep than in 1969. Wage and salary incomes in particular continued their rapid advance. Conditions on the labour market remained very tight at first, especially as regards skilled labour, in major branches of the economy, so further, considerable increases in wages and salaries were obtained relatively easily. The rate of increase of hourly wages in industry and commerce—which had already speeded up perceptibly in the course of 1969—was 7.8 % from 1 January to 1 October 1970; this is the highest rate recorded in a nine-month period since 1957/58 (disregarding wage rises conceded after the social crisis of May 1968). An increase of approximately 12 % in income from wages and salaries can be reckoned with for 1970 as a whole, even allowing for the fact that the total number of hours worked did not increase as much as from 1968 to 1969, owing to the increasingly widespread tendency to cut the working week. Transfer incomes probably grew at least as fast, while household income from entrepreneurship and property increased more slowly. Household income available for consumption increased somewhat more than gross income thanks to the perceptible reduction in the incidence of taxation, more especially in the second half of the year.

The marked discrepancies between supply and demand which had been a feature of 1969 eased only very slowly in 1970. According to reports from industry, capacity bottlenecks and labour shortages were still almost as serious at the beginning of the summer as at the end of 1969, although a clear differentiation between branches was taking shape. At this time, for instance, the situation had already largely eased in the traditional and export-remote consumer goods industries, where there is a decline in the inflow and backlog of orders. On the other hand, capacity utilization remained at a very high level in the capital goods industries—and also in the motor vehicle industry—where new orders continued to run ahead of supply possibilities. As a result, production growth conditions varied very considerably from one branch to another. The output of consumer goods even dipped for a time, and a firmer upward trend only reappeared in the autumn. The production of capital goods continued to expand, within the more or less narrow limits set by capacities. The trend in the basic materials industries remained very buoyant in the first half of the year, but the inflow of orders—more especially for iron and steel products—slackened markedly in the summer months and after. All in all, industry's

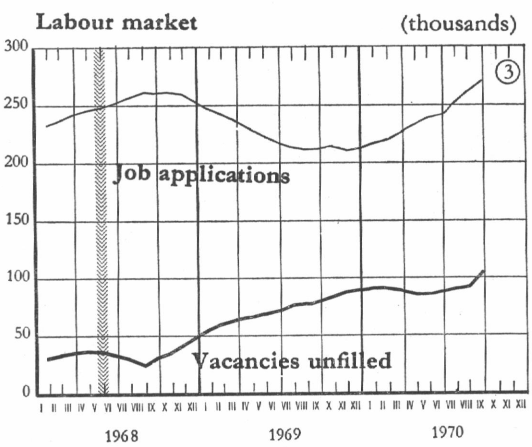


contribution to the GNP in real terms probably showed a year-to-year increase of about 7 %[1]. Building and construction doubtless did not increase quite so sharply, especially as it was hampered at the beginning of the year not only by the hesitant demand for new dwellings but also by unusually bad weather. But even

[1] The monthly INSEE index of industrial production only covers the output of the basic materials and consumer goods industries and therefore gives the 1970 trend very imperfectly (see Quarterly Survey No. 2/1970, p. 42).

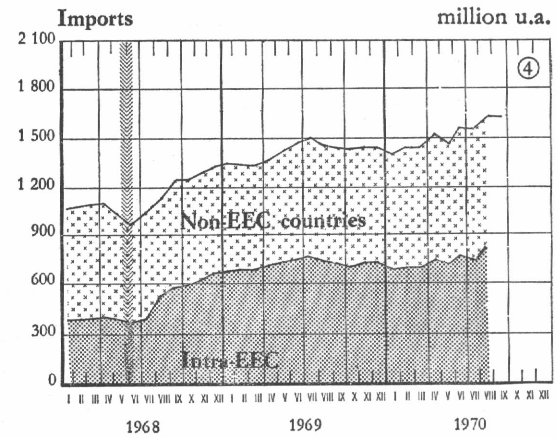
assuming that the advance in parts of the services sector was very slow at times and that agricultural production may well have been hardly higher than in 1969, the real gross national product, which grew by about 7.9 % from 1968 to 1969, probably grew about 6 % from 1969 to 1970, whereas after the devaluation a growth rate of some 3 ½ to 4 % had been considered compatible with the aims of the stabilization policy.

In year-to-year terms, the advance in productivity was significantly smaller and the tendency to cut the working week was stronger. This growth therefore led to the recruitment of additional workers, more especially in industry and in the services sector. The result was a further appreciable increase in the number of persons in paid employment, particularly in the first half of 1970. The labour force increased faster, as a result of a rise in the proportion of persons earning or seeking to earn wages



or salary and of a sharp upsurge in immigration, but firms still found it fairly difficult to recruit suitable personnel. At all events, there was a further increase in the number of unfilled vacancies during the year. Concurrently, however, the number of persons seeking employment also showed a distinct tendency to rise[1]. It would appear that the structure of available manpower reserves was still insufficiently in line with the requirements of the economy. In some branches there may also have been a measure of frictional unemployment at times.

Domestic supply was increasingly supplemented by buying from abroad during the year. The volume of visible imports, in fact, picked up unmistakably after the marked decline, particularly affecting raw materials and consumer goods, which followed devaluation and persisted into the first quarter. Halfway through

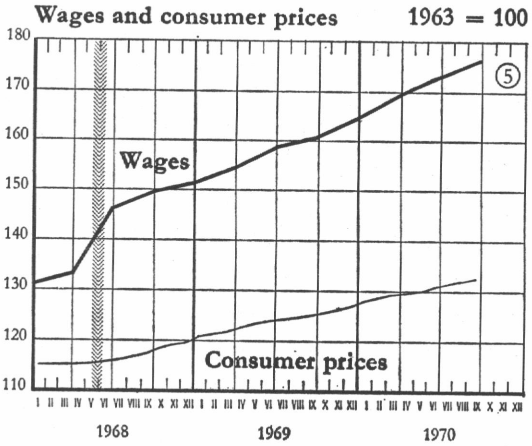


the year, the volume of visible imports—calculated from foreign trade statistics and seasonally adjusted—was already 13 % higher than at the end of 1969, the increase in imports of energy and fuels and of raw materials and semi-finished goods being particularly high. But, for 1970 as a whole, the increase on 1969 in the volume of visible imports will doubtless only be about 8% (as against 21.4% from 1968 to 1969). Purchases in the services sector probably also rose more strongly again, especially in the second half of the year after the foreign exchange allowance for travel abroad was increased.

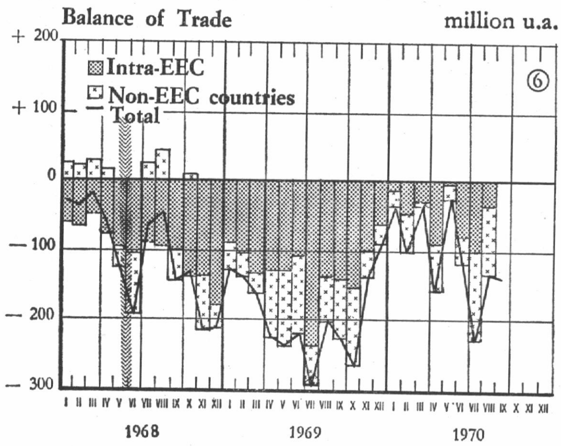
Supply undoubtedly showed a tendency to become more elastic and the pressure of demand on major domestic markets eased unmistakably, but the trends of demand in monetary terms and of supply in real terms remained very divergent well into the summer. Not until later in the year did the price rise probably flatten out slightly, as the impact of devaluation was gradually absorbed, and more particularly because of a better supply position on the food markets. At producer level, the prices of indus-

[1] A comparison of labour market statistics for different periods is, however, hampered by the continuous extension and improvement of the recording of job-seekers and unfilled vacancies, following the establishment of a national employment authority (Agence nationale de l'emploi).

trial products were driven up quite considerably in the early months of the year—at an annual rate of more than 7%, according to the information provided by businessmen—through the combined effects of worldwide inflation; the devaluation, which made imports even dearer; the rise of costs, notably wage costs; and a level of demand which made it possible to pass these burdens on and perhaps even increase profit margins as well. The prices of agricultural products also rose very markedly, since supply was inadequate and phased realignment on Common Market prices was necessary after the devaluation. At consumer level, in addition, the faster rise of prices for services—only partially attributable to the higher charges for public services—made itself especially felt. All in all, according to the INSEE index of 259 items the cost of living in September 1970 was 4.3 % higher than in December 1969 and 5.7% up on the twelve months.



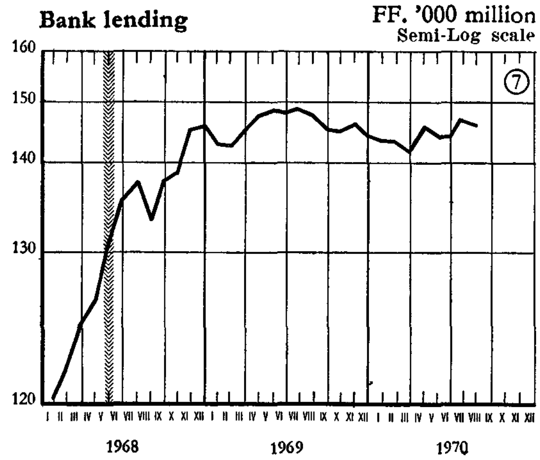
So there were hardly any signs of progress towards stabilizing costs and prices until well into 1970. In contrast, the drive to re-establish external equilibrium achieved quick results. Soaring exports and the initially continuing hesitancy of imports led to a substantial improvement in the trade balance. According to customs returns the deficit, which had reached FF 9 380 million in the first nine months of 1969, shrank to FF 5 410 million in the corresponding period of 1970. Furthermore, renewed confidence in the franc swung "leads and lags" in favour of France and considerable amounts of capital flowed back into the country, so that the balance of payments, which had closed with a deficit of about $1 660 million in 1969, moved more and more into the black and probably produced a surplus of some $1 700 million between the end of December 1969 and the end of September 1970. This enabled the monetary authorities to rebuild their gold and currency reserves and at the same time pay off promptly, even before mid-year, all the debts they had incurred with foreign central banks and domestic commercial banks during the balance of payment difficulties of 1968/69. Official net reserves, down to only $1 290 million at the time of the devaluation, climbed back to about $4 000 million by the end of October 1970.



The strong expansionary impact of the increasing inflows of foreign currency on internal liquidity was largely neutralized, at least till mid-year, by the restrictive credit and budget policy. The result was that although the supply of money (notes and coins in circulation, sight and time deposits) accelerated slightly after the spring it still only increased 5.7% on balance in the first eight months of 1970, as against 4.5% in the corresponding period of the previous year; at the end of August it was only 7.3% up on the twelve months. The money supply thus increased substantially less in France than in the other EEC countries. Indeed, there was not even a rise of 1½% on August 1969 in money availabilities proper—that is to say, excluding time deposits, which were pushed up by, in particular, more intensive savings promotion and showed a considerable increase. Cash transactions by the public authorities especially tended to neutralize the inflow of foreign money; they took almost FF 1 000 million of liquidity out of the economy in the first eight months of

1970, after pumping it in to the amount of FF 7 100 million in the same period only a year before. Budget management, in particular, was very restrictive—a cautious policy on expenditure and unusually high tax receipts produced a cash surplus of approximately FF 1 000 million by the end of July, compared with a deficit of FF 6 100 million in the first seven months of 1969.

Furthermore, although bank lending to firms unmistakably gathered momentum from the second quarter onwards, it continued relatively moderate on balance in the first eight months, mainly because short-term loans remained subject to a strict quantitative control and the penalties for exceeding the credit ceiling were increased from March. Total loans at the end of July 1970 were only 9½% higher than a year earlier.



Demand for and supply of goods and services

	1968 [1]	1969 [1]		1970 [2]		1971 [3]
	At current prices (in FF '000 million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports [4]	90.8	+ 14.9	+ 20.4	+ 15½	+ 25½	+ 8½
Gross fixed asset formation	157.2	+ 10.1	+ 17.1	+ 8	+ 15½	+ 6
Public current expenditure on goods and services	79.9	+ 3.6	+ 11.6	+ 3	+ 11	+ 3½
Private consumers' expenditure	383.5	+ 7.2	+ 14.3	+ 4½	+ 10½	+ 5½
Gross national product	628.5	+ 7.9	+ 15.5	+ 6	+ 12	+ 5½
Imports [4]	90.4	+ 18.2	+ 25.9	+ 7	+ 18	+ 9

[1] Rapport sur les Comptes de la Nation 1969, Ministère de l'Economie et des Finances, Paris.
[2] Commission estimates.
[3] Commission forecasts.
[4] Goods, services and factor income.

Note :

(a) The difference between the figures for demand and those for supply is accounted for by movements in stocks.
(b) The estimates and forecasts are approximations based on certain hypotheses, worked out by the Commission and generally mentioned in the Quarterly Surveys. They have been discussed with the experts from the member countries but are established and published on the sole responsibility of the Commission.

Although the monetary authorities also made more use of their liquidity instruments and repeatedly increased the minimum reserves which banks were required to hold, the money market eased fairly noticeably in the course of the year. The call-money rate, after rising steadily throughout 1969 and attaining a peak of 11% on 26 December, fell even below Bank rate (8 %) at times in the period up to the end of July and the beginning of August 1970. Admittedly, this tendency was strengthened by the intervention policy of the Banque de France, which was mainly aligned on the movement of rates on the Eurodollar market. Bank rate was reduced to 7.5% on 27 August 1970 and, following a further easing of interest rates, to 7% on 20 October.

But the downward tendency of interest rates hardly penetrated to the capital market. The real yields of fixed-interest securities admittedly dropped slightly from March, but new issues continued to carry a relatively high rate of interest, despite the fact that the abundance of capital available for investment made the placing of even large loans quite easy. Stocks and shares to the value of almost FF 13 900 million found takers in the first eight months of the year alone, as against FF 10 900 million in the corresponding period of 1969. Public authorities and the public savings institutions were among those who resorted to the capital market much more heavily than a year earlier.

2. Outlook for 1971

The year 1970 clearly saw the end of the French economy's post-devaluation phase, which was characterized by the effects of the restrictive credit policy pursued since the end of 1968 and of the rigorously implemented budget reorganization following the devaluation, and by a uniquely favourable conjunction of very dynamic foreign demand with an increased propensity to save of the French consumer. Developments in 1971 will probably be marked by a different pattern of demand, for there are many signs that the growth of production and employment will be fostered less by exports and more by domestic demand.

It was already apparent in the closing months of 1970 that foreign demand was beginning to lose momentum. Export industry reported a smaller inflow of orders and a slower increase of turnover. The slowdown of economic activity in major purchasing countries to be expected in 1971, and the gradual curbing of international inflation, will have an adverse effect on foreign sales conditions even though, as stated elsewhere in this survey, the prospects for world trade as a whole are not unfavourable. It may be added that devaluation still provides the French economy with an adequate competitive margin, despite the subsequent increases in costs. It is always possible, however, that the propensity to export will decline in so far as the home market recovers and, above all, offers easier sales prospects. The ultimate result is likely to be that the growth of exports to the EEC countries in particular will level off but also that the rise of exports to the rest of the world will drop well below the exceptional rates recorded to date, despite the gradual recovery of the business situation in America.

As regards the upward pressures on the economy the emphasis will shift unmistakably to domestic demand, and within domestic demand to consumption.

Gross fixed asset formation will probably continue to increase at more or less its recent rate. The propensity to invest of enterprises has, in fact, remained very high so far—at any rate higher than was to be initially expected in view of the fact that the flurry of capacity expansion and rationalization has now lasted more than two years. The increase in expenditure on new construction and plant and machinery planned for 1971 may be attributable to some extent to investment projects which had already begun but had been held up by delivery bottlenecks. However, it also seems that enterprises are still optimistic about longer-term profit and sales prospects. Firms in private industry, for instance, plan a further 20% increase on 1970 of their fixed investment, while public enterprises—which invested relatively little in 1970—also expect their capital expenditure to increase noticeably in 1971. Furthermore, State capital expenditure should increase more, if anything, in the course of next year. Finally, a progressive recovery can be expected in residential construction—the number of building starts had already picked up again in the second half of 1970, thanks to the relaxation of controls for certain construction and mortgage loans and the release of more public funds, and an additional increase in low-cost residential construction was planned for 1971.

As against this, it is hard to assess what impact investment in stocks will have in 1971. There is considerable evidence that stocks in industry and commerce had largely settled at a "normal" level by the end of 1970. This implies that their increase in 1971 should depend mainly on the needs of current production and turnover. But agricultural stocks, which were considerably run down in 1969/1970, may well rise more steeply again if harvests are normal.

There is no doubt that expenditure on consumption will increase at a noticeably faster rate in 1971 and thus replace the export boom as a crucial factor in economic growth.

Public current expenditure is likely to show a particularly steep increase, not only as a result of greater purchases of goods and materials but also, and more especially, because unexpectedly sharp increases in living costs had already led to additional wage and salary increases at the end of 1970 and further claims for backdated increases are pending which will probably exert their full effect in the 1971 budget year.

The growth of private consumers' expenditure can also be expected to gather momentum sharply, as incomes continue to forge ahead and the propensity to save weakens. It can, in fact, be assumed that households will again devote a larger proportion of their disposable income to consumption, now that they have largely reconstituted the savings which they used in the 1968/1969 monetary crises, more particularly to buy consumer durables and hire purchase provisions have been perceptibly eased. Furthermore, the fairly considerable tax reliefs scheduled for 1971 should do much to offset the slowdown of the increase in household gross income which may be expected to occur if there is a real slackening of the wage and price rise.

This trend of the various components of demand will ensure that domestic production again grows fairly sharply. In year-to-year terms, the increase will probably be somewhat smaller than from 1969 to 1970, but the rate of growth may well increase, rather than otherwise, in the course of the year. Greater supply elasticity is to be expected for industry in particular, owing not only to the extensive investments of 1970 but also to more even utilization of the production apparatus—declining demand pressure on the export and capital goods industries and increased utilization of capacity in industries near the consumer stage. If seasonal variations are left out of account, production in building and construction should also accelerate if anything, since, as already mentioned, residential construction demand can be expected to gradually provide a positive spur once again. Finally, if we assume that there will be a further fairly steady overall increase in the services sector and that weather conditions for agricultural production will be normal, the growth of the real gross national product from 1970 to 1971 can be put at about 5½%.

In view of the productivity gains to be expected and the pronounced tendency to reductions in the working week, this growth would require a further increase in the number of persons at work. But it is probable that the increase in the labour force will lose momentum and that the occupational qualifications and regional distribution of the labour supply will continue only inadequately to satisfy demand, despite the significantly greater endeavours which the authorities and the two sides of industry have been making for some time to improve vocational training and to speed up retraining. So it is likely that in 1971 the labour market as a whole will again be characterized by a relatively large number of job-seekers and persisting tightness in some areas.

Imports have already shown a firmer upward trend in the second half of 1970, in line with domestic demand and domestic production. They will go on increasing rapidly in 1971, especially since foreign suppliers may well be induced to show greater interest in the French market by the expected slowdown of domestic business activity in major industrialized countries.

A further improvement in the balance of trade is hardly to be expected under these circumstances, even if the terms of trade—which were relatively bad in 1970, in the aftermath of devaluation—take a turn for the better. It would appear that the external surplus (as defined for national accounts) will settle at its present level at best, but is more likely to contract.

Although this means that hardly any—or at least, very much less—inflation is likely to be imported in 1971, a speedy stabilization of the price level, which rose about 6% in 1970 (as measured by the GNP "deflator"), is not very likely for the moment. The internal upward pressures are obviously diminishing only very slowly. Cost rises, in particular, remain appreciable. It is true that increases in agreed wages may not run so far ahead of the simultaneously attainable productivity gains in 1971 as previously, but the wage drift—partly in the form of backdated payments for 1970—will doubtless remain fairly marked. Furthermore, allowance must be made for a new cost factor—the rapidly increasing switch to salaried status for industrial workers, entailing, among other benefits, continued payment of wages in cases of sickness. Entrepreneurs may be all the more tempted to pass these cost increases on to the domestic buyer as their previous above-average profit margins in foreign business come under pressure. In the services sector, structural factors are also exerting an upward pressure on prices, quite apart from the fact that increases in charges for public services are already scheduled and that a further increase in controlled rents is probable. It is therefore to be feared that the rate of price increases, as measured in terms of the gross national product, will hardly drop below 4%—in other words, it will remain perceptibly above the rate of increase given as a guideline for the price trend in the draft third Medium-term Economic Policy Programme of the Community.

As regards short-term economic policy, these prospects mean that it is necessary to continue the policy of economic consolidation for the time being and to facilitate further relaxation of tension which got under way in 1970. For experience shows that costs and prices can hardly be stabilized on a lasting basis after a relatively long phase of inflation without the pace of aggregate economic growth being lower than that of capacity expansion for a while. The quickest possible re-establishment of cost and price stability should remain a priority objective at present, precisely in the interests of long-term, lasting preservation of growth and full employment.

Under the circumstances, attainment of optimum stability and growth in 1971 will probably require above all a continued cautious regulation of demand by budget policy. The expenditure appropriations in the draft finance law for 1971 submitted by the Government allow for this requirement. Definitive expenditure is only to be 8.7% higher than in the 1970 budget, i.e. even something below the Government's estimate of 9% for the increase in gross domestic production. The increase is hardly more than 9 % even if "temporary" expenditure, that is to say investment grants and loans, long-term export financing, etc., is included. The slight increase in the growth of expenditure over that estimated in the 1970 budget (6.3%, the initially expected increase in the value of gross domestic producction also being 9%) seems acceptable since almost half of it is due to the renewed increase of capital expenditure. The fact remains that purely administrative expenditure again shows a bigger absolute and also relative increase—12.8 %—than any other item in the draft budget. This is the first budget since 1963—excluding the one for 1969—to contain such a high rate.

However, the public authorities may well give a greater stimulus to economic expansion in 1971 than these figures would suggest. Considerable transfers of credits from 1970 will probably have to be coped with in the 1971 budget year, and certain items of expenditure—more especially those for wages and salaries—seem to have been assessed very much on the low side. But, quite apart from these factors, it must also be remembered that authorizations to spend appropriated funds, after having been reduced in 1970, will increase markedly in 1971, so that additional orders for capital goods and building and construction are to be expected.

The increase in aggregate revenue is in line with the proposed increases in expenditure so that the draft budget—as in 1970—is balanced.

In principle, a surplus of about FF 3 000 million could have been achieved if the Goverment had not proposed tax reliefs of about this amount. Following the reduction in the tax burden—more especially for the lower income groups—by the finance law of 1970, it is proposed to make a further reduction in 1971 by cutting and standardizing income tax rates, abolishing the supplementary tax introduced in 1960 and dropping various surtaxes. It is estimated that all this will reduce tax yields by almost FF 3 200 million and increase the disposable incomes of households by more than ½%. These tax reliefs aim at distributing tax burdens more equitably, and must therefore certainly be seen from the social policy angle; but—in view of the fact that the propensity to consume is picking up again anyway and of the income trend expected for 1971—it must be asked whether they are fully consistent with the requirements of short-term economic policy. When it comes to reducing the incidence of taxation on households more preference might perhaps be given to scaling down indirect taxes. Such an approach not only has the advantage of exerting a direct inhibiting effect on prices, but also fits in better with the medium-term plans for a comprehensive tax reform aimed at shifting the emphasis from indirect to direct taxation. It would also be in line with the endeavours to harmonize rates of value added tax in the Community.

Everything should be done to go on encouraging households' propensity to save, so as to minimize the impact of the tax reliefs on consumption under present conditions. Good results have been achieved by the measures already taken in this connection—more especially under the stabilization programme at the end of 1969 and the beginning of 1970—such as higher interest rates for savings deposits and introduction of a new building savings system. But additional incentives might well be advisable, in particular for saving through securities. One possibility here would be to help formation of assets by workers on a more lasting basis by exempting the capital saved from income tax. At the same time, a larger supply of private savings would help non-inflationary financing of the investments required by the economy. This would be all the more desirable in 1971, since the financing surplus of the public authorities will contract sharply, while the financing needs of firms will increase faster.

The monetary and credit policy should keep to its basically restrictive course until greater cost and price stability has been achieved. The abolition of the credit squeeze—which had already been perceptibly relaxed half way through the year—approved by the Conseil national du Crédit at the end of October is in no way inconsistent with this requirement, as it had become increasingly clear that a direct credit control has considerable disadvantages if it is maintained over a fairly long period of time. It distorts competition between credit institutions, makes for an irrational distribution of scarce funds, and changes the credit structure, quite apart from the fact that its efficiency is impaired because lenders and borrowers can find too many ways round it, particularly when it is selective. It was therefore obvious that preference should be given to greater use of interest and liquidity instruments, more especially the latter.

The determination of the monetary authorities to keep the credit trend in line with short-term economic policy by these means is shown by the other measures they have taken concurrently with the latest adjustment of Bank rate to the international interest trends and the abolition of the quantitative credit controls. In particular the reduction of the commercial banks' opportunities for rediscounting with the Central Bank, which were previously often regarded as automatic, should lead to greater scarcity of credit, and also tend to make it dearer in so far as the banks turn to the money market as an alternative source of supply. There are also plans for extending and improving the minimum reserve system. So far, the reserves to be held interest-free by the Central Bank have been calculated solely on the basis of the customers' deposits administered by banks, the result being that the deposit banks were relatively heavily burdened while the finance institutions, which receive no deposits from the public but nevertheless participate in the financing of loans, were hardly affected at all. In future, however, the loans granted to businesses and the private sector will also be subject to the formation of minimum reserves. This will undoubtedly give the monetary authorities greater scope for influencing the trend of credit in line with market requirements and facilitate a flexible adjustment of monetary and credit policy to the current economic data.

Major economic policy measures

June

(1) At the end of the month the Conseil national du Crédit decided on a marked relaxation of the credit policy: the quantitative restrictions dating back to November 1968, initially

introduced for a very short specific period but subsequently extended and tightened up repeatedly, were dropped with effect from 1 July for medium-term investment credits rediscountable with the Banque de France under current arrangements, for short-term harvest financing credits and certain medium-and long-term loans of the Crédit agricole, and for residental building loans from building savings funds; the restrictions were also eased substantially for short-term export credits, mortgages and medium-term rediscountable building loans. But the grant of other credits to business and personal advances, notably short-term, remains subject to a stringent ceiling in the second half of the year: the volume outstanding at the end of December 1970 may not be more than a bare 3% above the figure for 30 June 1970.

(2) The interest rate for savings deposits with savings and other banks was raised from 4% to 4¼%, as a further incentive to save. In addition, a fidelity premium of ¾ % was granted for savings bank assets under certain conditions.

July

(1) In accordance with the law of 2 January 1970, the "minimum growth wage" (SMIC) was increased as from 1 July by 4.16%, from FF 3.36 to FF 3.50 per hour, in the light of the latest price rises and the general wage trend; this brought it to 11.1 % above the level in the corresponding period of 1969.

(2) The value added tax on television sets was reduced from 33% to 23% with effect from 1 July. This should allow a reduction of about 8% in the retail price.

(3) Public unemployment benefits and allowances for partial unemployment were increased by 6% to 7% with effect from 6 July.

(4) Further increase, with effect from 10 July, in the minimum reserves which the banks are required to hold—the rate for sight deposits being raised from 6½% to 7½% and the rate for time deposits from 1½% to 2½%. This should lead to a reduction of about FF 1500 million in bank liquidity, which had shown a further substantial increase in recent weeks as a result of the persisting inflow of foreign currency.

(5) The Government decided to support expansion by releasing FF 1100 million—more especially for residential and road building and education—from the appropriations under the 1970 budget which had been frozen initially in the economic action fund. Concurrently, a decree of 4 August published additional expenditure authorizations of FF 1400 million from the 1970 budget.

(6) In early July the French employers' association (CNPF) and the unions signed an agreement on training and further training entitling about 8 to 9 million persons in paid employment in industry and commerce to train during working hours without loss of income. The costs were to be met partly by enterprises and partly by the public authorities.

(7) The obligation of commercial banks to deposit the dollar counter-value of their foreign assets with the Banque de France, which had already been noticeably eased at the end of April, was completely abolished at the beginning of July.

(8) Halfway through the month, the Government decided on various reforms of the social security system, mainly in order to curb the increase of expenditure by the public health insurance funds (reorganization of the hospital system and relationships between social insurance institutions and doctors, reduction in prices of medicines and in fees for laboratory examinations, reduction in the profit margins of dispensing chemists, etc.). Concurrently, a considerable improvement in certain social security benefits was announced (reform and increase of children's and family allowances, introduction of an allowance for orphans, increase in widows' pensions and old age payments).

August

(1) Exchange controls were substantially eased at the beginning of August, more especially for foreign travel: French tourists are now entitled to take up to the equivalent of FF 1500 in foreign currency per trip abroad (two journeys per year) and can also export up to FF 500 in banknotes (previously FF 1500 in foreign currency per year and FF 200 in banknotes). The foreign currency allowance for travellers on business

was increased to FF 400 per day or FF 4000 per journey in foreign currency (previously FF 200 to 300 or FF 2000 to 3000, depending on the country). At the same time there was an increase in the sums which may be sent abroad without special authorization, more especially for investment expenditure.

(2) After clear tendencies for interest rates to sink and spread to the French money market, owing to heavy inflows of liquidity from abroad and the international interest trend, the Banque de France decided on 27 August to cut Bank rate from 8 % to 7.5 % and the rate for advances against securities from 9.5 % to 9 %. Simultaneously, there was a reduction from 8% to 7.5% in the discount rate for short-term claims resulting from foreign business and for medium-term claims resulting from foreign business with EEC countries. The preferential discount rate for medium-term claims resulting from foreign business with non-member countries remained unchanged at 4%.

September

At the beginning of September the Government approved general guidelines for the tax policy of the next five years. The whole tax system is to be thoroughly modernized so as to increase the relative importance of direct taxes, which currently provide only about a third of the aggregate tax yield, and to reduce the share of indirect taxes from two thirds to 40%. As regards direct taxation, it is planned in particular to iron out the differences between the incidence of taxation on the self-employed and on the employed. It is also planned to do away with various tax privileges enjoyed by farmers and professional men, to make tax evasion more difficult by carrying out more frequent checks on enterprises, and to ensure that tax receipts come in more quickly and can be adjusted more easily to the economic situation by introducing pay as you earn for wage earners or monthly advance payments. As regards indirect taxation, it is intended to reduce the number of value added tax rates from the present four to two —abolishing the 33.3% rate, gradually reducing the normal rate from 23% to 17% or 18%, and applying the 7.5% rate in particular to food, which in some cases still attracts 17.6%.

October

(1) Hire purchase provisions, which had already been repeatedly eased since spring, were further relaxed in early October: the cash down-payment for private cars was reduced from 50% to 40 %, for caravans from 40% to 30%, and for household appliances and machines from 25% to 20%; the repayment period, up till then usually 18 months, was lengthened to a standard period of 21 months.

(2) Halfway through October, the Government submitted its draft finance law for 1971 to the National Assembly. As in 1970, the budget is balanced, with aggregate expenditure increasing by 9.2%, which is not more than the expected increase in the value of domestic production, and an estimated increase in revenue of the same order of magnitude. In detail, the following changes are proposed vis-à-vis the previous budget: a 12.8% increase in civil administrative expenditure (1970, +9.8%), a 6.2% increase in military expenditure (1970, +4.7%) and an 8.9% increase in civil capital expenditure including investment loans and grants (1970 — 3.6%). Revenue is expected to be reduced more than FF 3500 million by the planned tax reliefs, with receipts from income tax dropping FF 3200 million and receipts from value added tax FF 300 million. The total tax yield in 1971 should nevertheless be 6.3% above the probable outturn for 1970, on the assumption that receipts from direct taxes will rise by 5.5% and those from indirect taxes by 8.2%.

(3) In view of the further reduction of interest rates on major international markets and the continuing relaxation on the domestic money market, on 20 October the Banque de France further cut its Bank rate by ½% to 7% and the rate for advance against securities by ½% to 8½%. A ½% cut was also made in the discount rate for short-term claims arising from foreign transactions, and for medium-term claims arising from foreign transactions with EEC countries. But the preferential discount rate for medium-term claims arising from foreign business with non-member countries was increased from 4% to 4½%.

At the same time, however, the Banque de France lowered, for the first time in thirteen years, the commercial banks' rediscount ceiling —by 10% for sums of up to FF 30 million and by 20% for larger sums. This reduced the *commercial banks' refinancing margin with the central bank by about FF 1300 million. The Banque de France also decided to add a penalty surcharge of ½% for the rediscounting of certain medium-term bills in the second year.*

(4) On 23 October the Conseil national du Crédit abolished, with immediate effect, the quantitative ceilings, which had already been markedly eased halfway through the year. Only loans for which the Treasury grants interest rebates remain subject to a quantitative control. To ensure more elbow-room for indirectly influencing the credit trend, however, it was decided to extend the compulsory minimum reserve system for commercial banks by calculating them on the basis of banks' advances as well as on sight and time deposits, which had previously been the sole criteria.

(5) Halfway through the month the Finance Minister, Mr Giscard d'Estaing, announced further measures to promote investment and export by enterprises: guarantees for private investment in the countries of the franc zone, reliefs for medium-sized enterprises which wish to export to the United States, and reforms of the medium-term investment and export credits system.

November

At the beginning of November the Government approved various regulations on the decentralization of administration. In particular the prefects of the regions and départements *were given greater powers with regard to investment decisions and the control of public expenditure.*

France

TABLE 1 : **Key indicators**

	1965	1966	1967	1968	1969	1969
	% change by volume on preceding year					Indices 1963=100
Gross national product	+ 4.7	+ 5.6	+ 4.7	+ 4.8	+ 7.9	139
Industrial production	+ 5.1	+ 7.7	+ 4.3	+ 4.5	+ 9.6	147
Total imports	+ 3.4	+ 13.9	+ 7.8	+ 12.7	+ 18.2	191
Private consumers' expenditure	+ 4.4	+ 4.8	+ 5.0	+ 5.6	+ 7.2	137
Public current expenditure on goods and services	+ 2.7	+ 2.1	+ 4.0	+ 5.6	+ 3.6	124
Gross fixed asset formation	+ 7.2	+ 8.9	+ 5.7	+ 7.3	+ 10.1	164
Total exports	+ 11.8	+ 8.4	+ 7.2	+ 10.3	+ 14.9	178
Gross national product per head of population	+ 3.7	+ 4.7	+ 3.9	+ 4.1	+ 7.1	133
Gross national product per person in employment	+ 4.3	+ 4.8	+ 4.4	+ 5.2	+ 6.7	134
	% change by value on preceding year					
Gross income per employee	+ 6.6	+ 6.1	+ 6.8	+ 11.9	+ 12.0	165

TABLE 2 : **Indicators for internal and external equilibrium**

	1965	1966	1967	1968	1969
Balance exports less imports					
in million u.a.	+ 1 012	+ 344	+ 425	+ 77	– 792
as percentage of GNP	1.0	0.3	0.4	0.06	0.6
Unemployment rate	1.3	1.4	1.8	2.1	1.7
consumer prices (% change on preceding year)	+ 2.5	+ 3.0	+ 2.8	+ 4.7	+ 6.6

TABLE 3 : Foreign trade (at current prices)

	% change on preceding year					Indices 1963=100	Million u.a.	% of totals
	1965	1966	1967	1968	1969	1969	1969	1969
Visible exports								
Total	+ 11.8	+ 8.3	+ 4.5	+ 11.4	+ 16.9	183	14 818	100.0
Intra-EEC	+ 18.0	+ 12.0	+ 2.0	+ 16.0	+ 29.9	229	7 082	47.8
To non-EEC countries	+ 7.8	+ 5.8	+ 6.3	+ 8.2	+ 7.1	155	7 736	52.2
Exports of food, beverages and tobacco								
Total	+ 11.4	+ 7.5	+ 2.9	+ 19.8	+ 20.1	203	2 543	17.2
Intra-EEC	+ 26.3	+ 19.4	+ 6.0	+ 26.6	+ 40.9	333	1 588	10.7
To non-EEC countries	+ 2.0	− 2.0	− 0.1	+ 12.8	− 3.6	123	955	6.5
Exports of raw materials, fuel and power								
Total	+ 4.4	+ 7.3	− 3.7	+ 1.6	+ 10.2	133	1 240	8.4
Intra-EEC	+ 8.9	+ 7.4	− 3.7	+ 0.9	+ 19.4	162	811	5.5
To non-EEC countries	− 1.8	+ 7.2	− 3.6	+ 2.6	− 3.8	99	429	2.9
Exports of semi-finished and finished industrial goods								
Total	+ 13.2	+ 8.7	+ 6.1	+ 11.1	+ 17.0	187	11 035	74.4
Intra-EEC	+ 18.3	+ 11.2	+ 2.3	+ 16.2	+ 28.4	222	4 683	31.6
To non-EEC countries	+ 10.3	+ 7.2	+ 8.5	+ 8.1	+ 9.8	168	6 352	42.8
Visible imports								
Total	+ 2.7	+ 14.6	+ 4.5	+ 12.5	+ 22.8	196	17 102	100.0
Intra-EEC	+ 6.7	+ 20.8	+ 10.7	+ 23.1	+ 30.0	275	8 600	50.3
From non-EEC countries	+ 0.3	+ 10.5	+ 0.2	+ 4.4	+ 16.3	152	8 502	49.7
Imports of food, beverages and tobacco								
Total	− 0.5	+ 8.4	− 2.6	+ 2.7	+ 19.1	147	2 287	13.4
Intra-EEC	+ 8.9	+ 1.3	+ 16.6	+ 31.8	+ 32.8	284	781	4.6
From non-EEC countries	− 2.8	+ 10.3	− 7.4	− 6.4	+ 13.0	118	1 506	8.8
Imports of raw materials, fuel and power								
Total	0	+ 5.9	+ 0.3	+ 3.6	+ 10.0	130	3 997	23.4
Intra-EEC	− 5.0	+ 9.5	− 2.3	+ 14.2	+ 11.2	134	670	3.9
From non-EEC countries	+ 0.9	+ 5.3	+ 0.8	+ 1.7	+ 9.8	129	3 327	19.5
Imports of semi-finished and finished industrial goods								
Total	+ 5.6	+ 22.0	+ 9.0	+ 19.6	+ 29.2	264	10 818	63.2
Intra-EEC	+ 8.6	+ 25.0	+ 11.9	+ 23.3	+ 31.8	304	7 149	41.7
From non-EEC countries	+ 1.5	+ 17.6	+ 4.3	+ 13.3	+ 24.5	211	3 669	21.5

TABLE 4 : Selected monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1963 = 100)	1968	*127.1*	*126.5*	*129.2*	*128.2*	*86.1*	*94.7*	*130.2*	*129.7*	*132.1*	*138.9*	*140.2*	*142.2*
	1969	*144.1*	*140.5*	*139.4*	*142.2*	*142.0*	*132.5*	*145.4*	*139.4*	*143.9*	*145.5*	*143.2*	*149.7*
	1970	*154.8*	*152.7*	*152.7*	*151.3*	*146.0*	*138.9*	*150.8*	*141.3*				
Number of persons seeking employment (1 000)	1968	*237.5*	*243.6*	*247.4*	*247.7*	*249.1*	*265.9*	*260.0*	*262.1*	*263.5*	*260.8*	*253.5*	*246.3*
	1969	*242.7*	*237.9*	*231.0*	*224.1*	*221.4*	*215.5*	*217.5*	*218.1*	*217.4*	*218.4*	*216.6*	*218.7*
	1970	*221.1*	*227.5*	*233.4*	*241.6*	*245.6*	*250.2*	*259.4*	*269.0*	*(283.5)*			
Construction : building permits issued for housing (1 000)	1968	*42.0*	*38.5*	*42.4*	*39.7*	*41.3*	*44.5*	*46.3*	*52.1*	*40.9*	*54.4*	*51.2*	*57.7*
	1969	*51.0*	*46.9*	*44.1*	*46.6*	*50.6*	*51.9*	*56.2*	*51.0*	*58.1*	*53.6*	*38.5*	*47.1*
	1970	*43.0*	*51.7*	*48.3*	*49.9*	*49.3*	*56.6*						
Private consumers' expenditure: turnover of department stores (1963 = 100)	1968	*127.1*	*128.0*	*129.8*	*124.5*	*89.9*	*123.8*	*142.7*	*143.7*	*134.8*	*141.2*	*161.6*	*143.0*
	1969	*146.3*	*139.2*	*143.0*	*139.0*	*150.9*	*138.6*	*146.1*	*153.8*	*137.1*	*142.8*	*143.9*	*147.0*
	1970	*153.3*	*141.3*	*139.7*	*138.4*	*142.6*	*141.0*	*144.5*					
Consumer prices (1963 = 100)	1968	114.9	115.0	115.1	115.4	115.8	116.2	116.6	117.1	117.9	119.1	119.5	119.8
	1969	121.1	121.5	122.1	122.7	123.2	123.6	124.2	124.5	125.1	125.9	126.5	126.9
	1970	127.9	128.5	129.0	129.6	130.3	131.0	131.5	131.7	132.2			
Visible imports (million u.a.)	1968	*1 086.9*	*1 102.8*	*1 097.9*	*1 101.3*	*909.5*	*917.8*	*1 307.5*	*1 205.1*	*1 227.4*	*1 315.4*	*1 348.0*	*1 342.9*
	1969	*1 362.7*	*1 317.0*	*1 278.4*	*1 470.9*	*1 461.0*	*1 473.3*	*1 573.6*	*1 377.9*	*1 462.6*	*1 540.3*	*1 375.6*	*1 400.8*
	1970	*1 431.8*	*1 485.6*	*1 399.7*	*1 663.4*	*1 339.4*	*1 690.4*	*1 660.9*	*1 622.9*	*(1 682)*	*(1 632)*		
Visible exports (million u.a.)	1968	*1 055.4*	*1 065.5*	*1 077.8*	*1 039.8*	*788.3*	*721.6*	*1 242.6*	*1 157.1*	*1 082.0*	*1 186.8*	*1 134.0*	*1 132.4*
	1969	*1 235.2*	*1 179.0*	*1 112.2*	*1 237.9*	*1 231.6*	*1 249.9*	*1 282.3*	*1 203.7*	*1 240.8*	*1 268.0*	*1 238.6*	*1 300.1*
	1970	*1 417.0*	*1 385.0*	*1 361.9*	*1 505.5*	*1 319.4*	*1 566.6*	*1 420.3*	*1 540.8*	*(1 611)*	*(1 470)*		
Balance of trade (million u.a.)	1968	*− 31.5*	*− 37.3*	*− 20.1*	*− 61.7*	*− 121.2*	*− 196.2*	*− 64.9*	*− 48.0*	*− 145.4*	*− 128.6*	*− 214.0*	*− 210.5*
	1969	*− 127.5*	*− 138.0*	*− 166.2*	*− 233.0*	*− 229.4*	*− 223.4*	*− 291.3*	*− 174.2*	*− 221.8*	*− 272.3*	*− 137.0*	*− 100.7*
	1970	*13.8*	*− 100.6*	*− 37.8*	*− 157.9*	*− 20.0*	*− 123.8*	*− 240.6*	*− 82.1*	*(−61)*	*(−162)*		
Official gold and foreign exchange reserves (million u.a.)	1968	6 053	6 014	6 023	6 027	5 720	5 517	4 850	4 601	4 374	4 265	3 985	4 200
	1969	4 215	4 125	3 986	3 774	3 636	3 610	3 594	3 781	4 006	3 913	3 989	3 833
	1970	3 885	3 957	3 961	4 032	4 142	4 282	4 492	4 545	4 576	4 617		
Money supply (FF '000 million)	1968	*192.3*	*193.1*	*193.1*	*193.6*	*207.6*	*207.0*	*203.0*	*204.3*	*207.9*	*209.0*	*209.7*	*211.5*
	1969	*207.9*	*210.6*	*212.7*	*214.5*	*211.4*	*212.3*	*212.7*	*213.4*	*213.8*	*211.8*	*212.5*	*210.3*
	1970	*208.7*	*209.3*	*211.1*	*213.3*	*212.4*	*213.5*	*215.4*					

France

NOTES TO GRAPHS AND TABLES

Source : Statistical Office of the European Communities (except as otherwise indicated). Conversion into units of account (1 u.a. = 0,888671 g of fine gold = US $ 1) at the official exchange rate.

Graph 1

— Exports fob. Series adjusted for seasonal variations; three-month moving averages.

Graph 2

— Industrial production : excluding construction, food, beverages and tobacco; indices adjusted for seasonal variations; three-month moving averages.

Graph 3

— Labour market; series adjusted for seasonal variations, three-month moving averages; position at end of month.

Graph 4

— Imports cif. Series adjusted for seasonal variations; three-month moving averages.

Graph 5

— Wages and consumer prices; index of hourly wage rates, all activities, all regions; national index of consumer prices (259 items).

Graph 6

— Balance of trade : difference between seasonally adjusted imports and exports.

Graph 7

— Bank lending; Source : Conseil National du Crédit; short-term loans (up to 2 years) from monetary institutions to business and private customers; end of period figures.

Table 1

Source : « Rapport sur les comptes de la Nation 1969. » Ministère de l'Economie et des Finances — Paris.

— GNP at market prices (new series on 1962 basis).

— Industrial production: value added by industry.

— Total exports and imports: goods, services and factor income.

— Gross income per employee: income from paid employment (including employers' share of social insurance contributions).

Table 2

Source : « Rapport sur les comptes de la Nation 1969. » Ministère de l'Economie et des Finances — Paris.

— Balance exports less imports: as defined for the national accounts.

— Unemployment rate: number of unemployed (persons available for and seeking employment, estimated on the basis of the number of job applicants, in the light of the latest population census) as percentage of the total domestic labour force.

— Consumer prices: implicit price index of private consumption computed from the national accounts.

Table 3

— Exports fob, imports cif; the products have been regrouped on the basis of the Statistical and Tariff Classification for International Trade (CST): food, beverages and tobacco (Groups 0 and 1 CST), raw materials, fuel and power (Groups 2-4 CST), semi-finished and finished industrial goods (Groups 5-9 CST).

Table 4

— Industrial production: adjusted for seasonal variations, excluding construction, food, beverages and tobacco.

— Number of persons seeking employment: seasonally adjusted figures, position at end of month.

— Construction: seasonally adjusted number of dwellings authorized.

— Private consumers' expenditure: seasonally adjusted indices of department store turnovers, constant samples.

— Consumer prices: national index of 259 items.

— Imports cif, exports fob, adjusted for seasonal variations.

— Balance of trade: difference between seasonally adjusted imports and exports.

— Official gold and foreign exchange reserves: gross reserves of gold and convertible currency held by the Banque de France and the Fonds de Stabilisation des changes at the end of month.

— Money supply: fiduciary circulation (total notes and coin in circulation, excluding notes and coin held by the Banque de France) plus sight deposits (deposits made with the Banque de France by private persons or enterprises, deposits with the Post Office giro or with public accountants, plus sight deposits relating to the activities of the banks within metropolitan France. Seasonally adjusted prices, at end of month.

C. Italy

Despite a very high level of potential demand, economic expansion lagged well behind expectations for most of 1970, mainly because of the continuing labour disputes. Big wage increases, together with a relatively slow growth of production, caused an upsurge of costs and prices from 1969 to 1970. Domestic demand in particular tended to expand fast, especially expenditure on consumption. However, despite difficulties in observing delivery deadlines, exports also increased significantly. As imports grew very fast because of the relatively limited elasticity of domestic supply, the deterioration on current account was exceptionally sharp. Nevertheless, the overall balance of payments developed much more favourably than in 1969, as a result of a considerable improvement on capital account.

If there is lasting peace on the labour front the economy should expand vigorously once again in 1971. From the angle of demand, at any rate—with the exception of building investment, which will probably tend to grow fairly slowly—the conditions are right for a fast increase in production and employment. The price situation will remain strained, so that the number one priority of economic policy, for the time being, must continue to be stabilization of prices and costs, since this is also of great importance in connection with consolidating the foreign trade and payments situation.

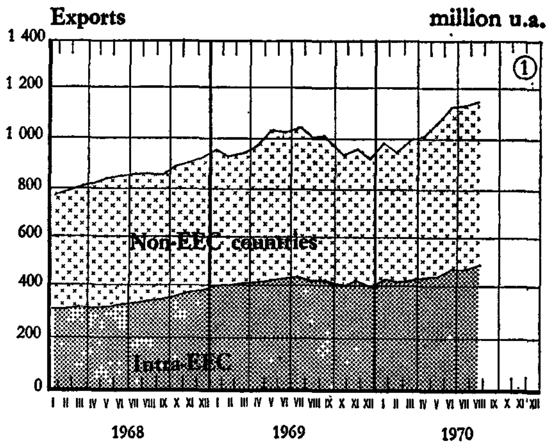
1. Balance sheet for 1970

Contrary to expectations, economic activity was fairly hesitant during most of the year, after an initial vigorous recovery following the sharp decline in the last four months of 1969 caused by strikes. The two decisive factors were certain technical difficulties of adaptation after the new 1969 wage agreements and, in particular, the persistence of labour troubles, which led to an appreciable hold-up of production. From the angle of potential demand, all the necessary conditions for sharper growth were present, but not until very late in 1970 does the trend of production seem to have become more lively.[1]

There were many factors which in themselves encouraged exports, such as the boom in the other member countries, renewed vigorous growth of world trade, revaluation of the German mark in the autumn of 1969, and further reductions of customs duties in leading non-member countries at the beginning of the year as agreed at the Kennedy Round negotiations. Nevertheless the curve of *visible exports,* while moving upwards vigorously, fell distinctly short of the trend. Contrary to what happened in the preceding years, Italy's relative share of intra-Community and world trade fell off. This was due chiefly to the inhibiting effects on production of the labour disputes referred to, as a result of which Italy's competitive position temporarily deteriorated, in particular as regards delivery dates. Until the beginning of the autumn at any rate, the monthly EEC Business Surveys showed quite a constant decrease in industry's backlog of orders from abroad, for the first time in seven years. As a whole, deliveries of visible exports to non-member countries increased somewhat more briskly than those

[1] Consequently, in the comparison for the full years some aggregates show rates of growth which are too high, owing to the method of calculation, and therefore mean little as a guide to the trend.

to member countries. Above-average year-to-year growth rates were registered in particular for exports of wine, precision instruments and footwear.



In 1970 total visible exports according to customs returns were an estimated 13½% in terms of value above the level of the previous year (1969, up 15.2%), which was exceptionally low at times. On the basis of the incomplete information available at present, exports of services seem to have grown appreciably, if more slowly than before.

Domestic demand, however, rose more rapidly, and faster than export demand, but the rate differed greatly from one item to another.

Gross fixed asset formation probably increased somewhat more sharply in money terms from 1969 to 1970, but in terms of volume it may have grown more slowly than a year earlier. *Building investment,* which accounts for about two thirds of total fixed asset formation, distinctly slackened off in the course of the year, but for statistical reasons it is still difficult at present to quantify this trend, which is found in building for commerce and industry and even more in residential building. The main reasons for it were the dying-out of the effects of administrative measures taken in 1967[1] and an easing of actual demand as a result of the sharp increase in building costs and growing financing difficulties. Public works, on the other hand, which had declined in 1969, recovered somewhat.

[1] See Quarterly Survey No. 3/4-1969, p. 68.

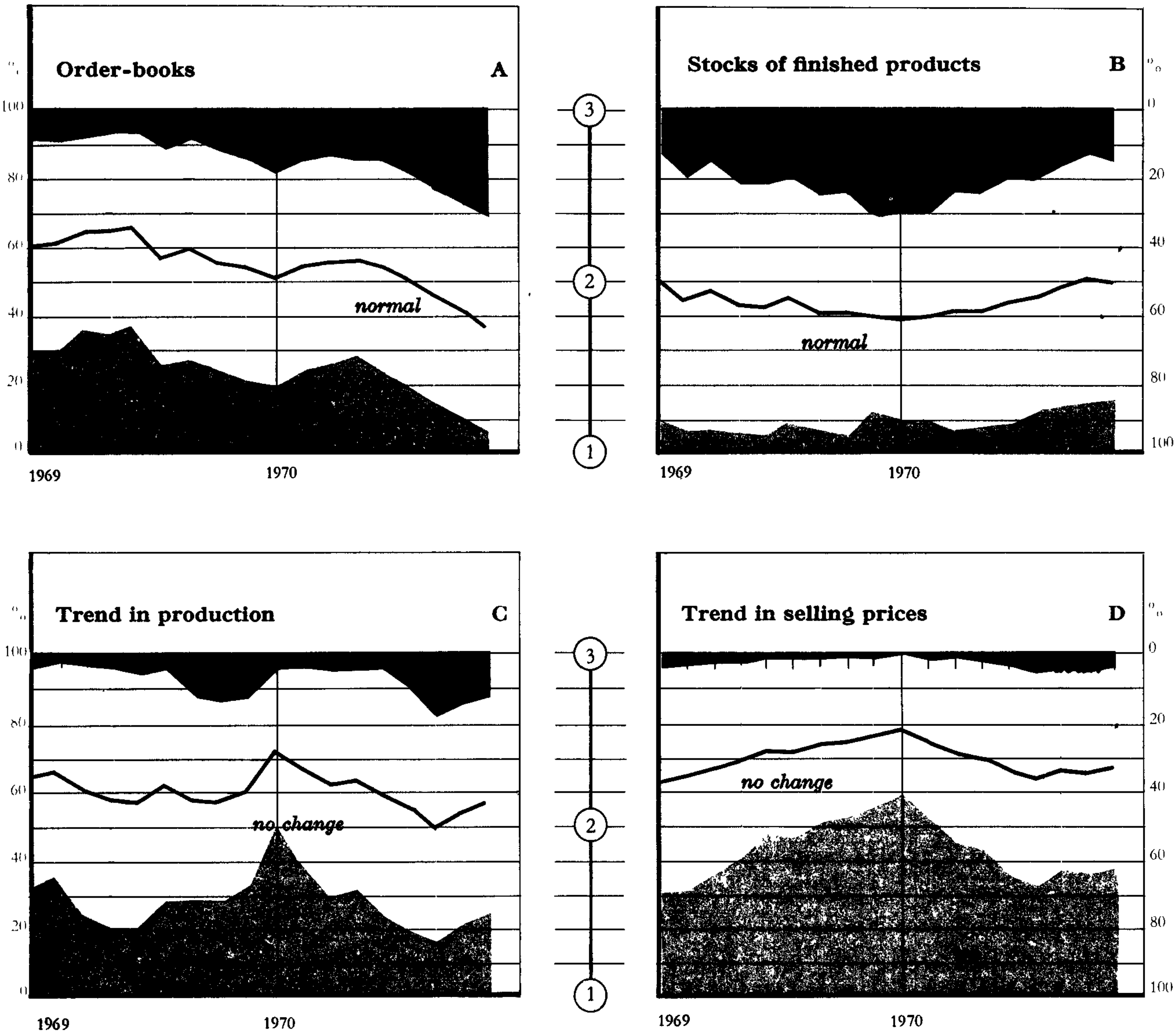
Despite considerable psychological and financial obstacles facing firms as a result of labour conflicts, *investment in plant and machinery* probably grew vigorously; endeavours to make good losses caused by strikes in the autumn of 1969 certainly played an important role here. At any rate, according to the results of the EEC Investment Survey of industry conducted in March and April (excluding enterprises run by public authorities), investments planned in industry, mainly in plant and machinery, were, in terms of value, at least 42% higher than in 1969. The promotion measures put into effect by the Government at the end of August may, furthermore, have given a new impetus to investment in plant and machinery in the final months of 1970.

After the exceptional rundown of stocks of finished products in 1969 and the first months of 1970, *investments in stocks* as a whole probably increased perceptibly once again from 1969 to 1970.

Consumer spending no doubt grew very vigorously. Private consumers' expenditure at least may well have accelerated considerably both as compared with 1969 and trendwise. For one thing, the savings ratio of households, which rose distinctly in 1969, may have dropped again in annual average terms. But above all gross wages and salaries grew exceptionally fast—by nearly 20%—as a result of new wage agreements concluded in leading industries (in particular chemicals, metal products, building and textiles), numerous increases in index-linked cost-of-living bonuses, a further alignment of wage zones, wage drift and an appreciable increase in the number of employed persons. This percentage is only a little below that registered in 1963. The rise in minimum hourly wages and salaries from December 1969 to January 1970 was even the fastest ever registered in Italy in a single month. Current transfer payments, too, probably continued to increase vigorously, though doubtless less fast than in 1969, when pensions were considerably improved.

Because of the reappearance of labour disputes, however, households seem for a time to have been relatively hesitant about making purchases. Furthermore, owing to bottlenecks in home production, their additional demand—for cars, for example—was largely directed towards

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Answers to the questions in the EEC business survey, carried out in Italy by ISCO-Mondo Economico.

GRAPHS A, B, C and D : The three colours (green, yellow and red) show the percentages of the three different answers.

The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows :

by 0.03 for the answer "above normal", or "up";
by 0.02 for the answer "normal", or "no change";
by 0.01 for the answer "below normal", or "down".

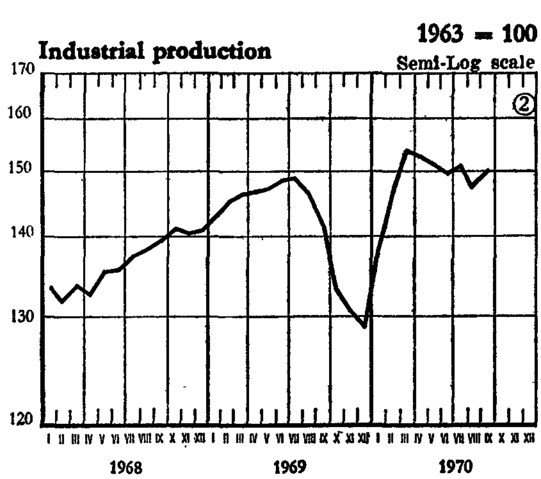
foreign products, which could be delivered faster. This is why, to judge by EEC Business Surveys, domestic orders in the consumer goods industries declined until well into the summer.

Total private consumers' expenditure may have risen from 1969 to 1970 by 14½% (1968 to 1969 : 8.8%).

There also seems to have been a distinct growth of public current expenditure on goods and services; as a result of efforts to make up for time lost through strikes it expanded very briskly, particularly in the early months of the year.

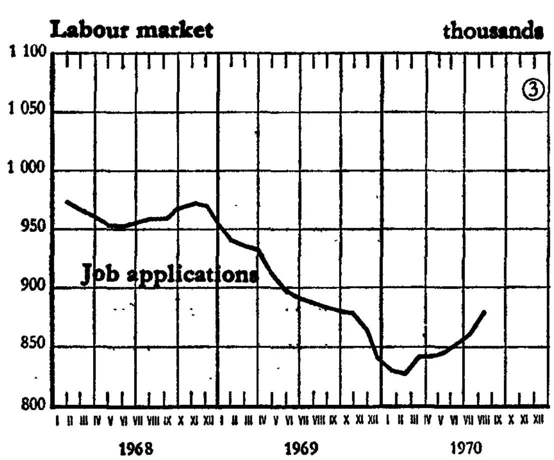
On the supply side, *agriculture's contribution in real terms* to gross national product has continued to grow vigorously. The decline in the production of cereals was more than offset by constantly increasing livestock production and, in particular, very abundant fruit crops.

Industrial production made distinct progress only in the first and last months of the year. In the interval progress was very hesitant, and in the second quarter there was even a decline. On the whole it was clearly below the level corresponding to the growth trend registered before the wave of strikes in the autumn of 1969. This was mainly due to recent labour disputes before the conclusion of the new wage agreements, chiefly in textiles, and to difficulties in applying the new rules on overtime. In individual cases, such as basic chemicals and steel, the growth of production may also have been held back because the limits of technical capacity have largely been reached. On account of the close links between industries, the year's trend in nearly all of them was more or less the same. For industrial production as a whole (contribution to gross national product at constant prices) an increase of approximately 8% is considered likely (4.3% increase from 1968 to 1969), while the rise in the index of production will probably be under 8%. Growth in building and construction, on the other hand, may well have been no more than sluggish in annual average terms (1969 : 9.6%).



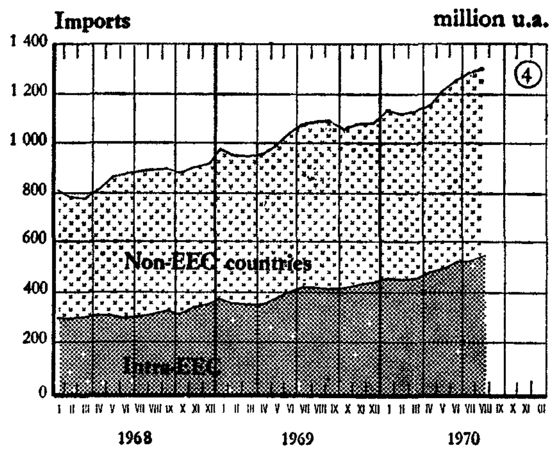
Owing to the sharply growing contribution of the services sector, *real gross national product* may have increased by about 6½% from 1969 to 1970 (5% in 1969).

Despite obstacles to production and despite the downtrend in the particularly labour-intensive building and construction industry, the number of *persons in paid employment* increased perceptibly, not only on the year-to-year basis (about 2% as against 1.6% from 1968 to 1969), but also in the course of 1970. The reduction in the agreed number of working hours in numerous industries, and the unwillingness of workers to do overtime, have certainly contributed to this trend.



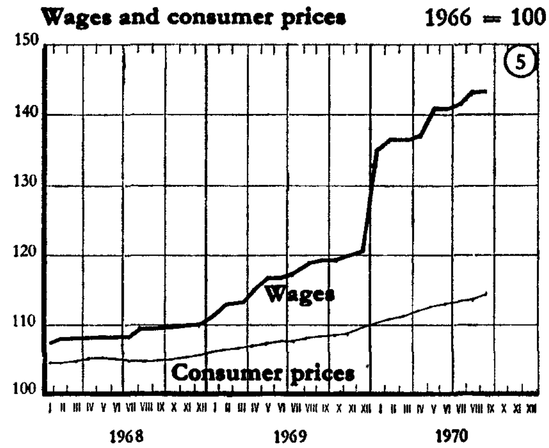
Towards mid-1970 the number of *unemployed* persons ceased to decline—doubtless temporarily—probably because of the strains between the two sides of industry and an increase in the labour force, which had been decreasing in recent years; this increase may have been caused partly by the rapid rise in wages. From 1969 to 1970, however, the number of unemployed definitely decreased (according to ISTAT figures by an estimated 8% as against 4.5% in the previous year) and the proportion of the labour force it represents may well have shrunk further (to about 3.2% compared with 3.4% in the previous year).

With the persistence of production bottlenecks and the accelerated expansion of total demand, *imports* grew very vigorously in 1970 too. During the year they seem to have expanded faster than in 1969. Visible imports according to customs returns may have risen from 1969 to 1970 by 21% in terms of value—approximately the same rate as in the previous year. The



highest growth rates were for imports of steel, motor vehicles, meat, plant and machinery and, geographically speaking, for imports from other Community countries. The expansion of imports of services was clearly even livelier than that of visible imports.

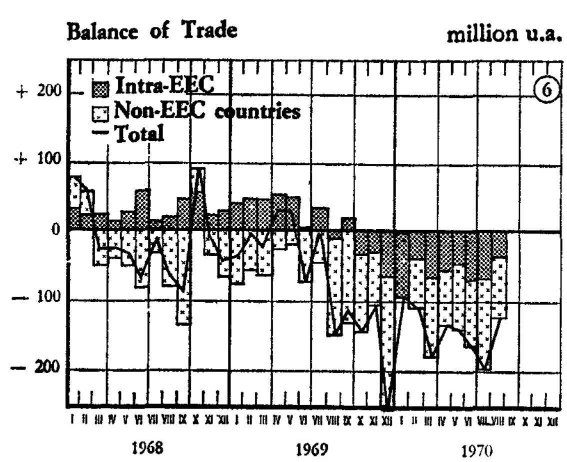
Prices continued to rise exceptionally fast in 1970, owing to strains in the supply/demand relationship and cost factors. Despite the declining building trend, the expansion of total demand in monetary terms considerably exceeded the growth of production, which was severely limited by special influences for a time. As regards the trend of costs, the rise in the prices of imported raw materials, at least, seems to have slackened. But a far more important factor, besides increases in numerous indirect taxes at the end of August, was the rapid increase in labour costs. Per capita wages and salaries may well have risen by an average of 18% or so in 1970; this was four times as fast as the expansion of overall productivity. The reductions in agreed working hours and a sharp in-



crease in the social burdens borne by firms also helped to raise costs.

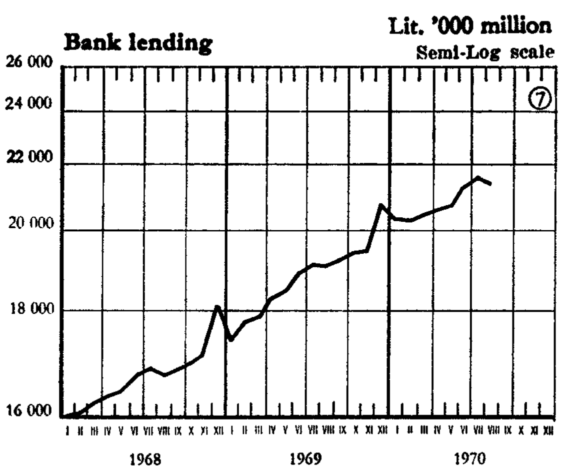
In the first nine months wholesale prices went up by 4.0% and consumer prices by 3.7%. In September they were respectively 6.4 and 5.0% higher than a year earlier.

Despite a considerable improvement in the terms of trade, the *trade deficit* continued to increase considerably (according to customs returns, from Lit. 450 000 million in 1969 to about Lit. 700 000 million). As, at the same time, there was a decline in net exports of services, which had still been growing the pre-



vious year, and in current transfer payments, the surplus on current account diminished sharply. On the other hand, capital account, which had shown an exceptionally heavy deficit in 1969, improved considerably, in the main because of numerous bond issues abroad, mostly at variable interest rates. The total reached in 1970 through this and other forms of indebtedness abroad far exceeded $1 000 million. Consequently, the deficit on the overall balance of payments has at least become appreciably smaller; in fact, it may even have given place to a small surplus. In the first eight months it stood at Lit. 18 500 million, compared with Lit. 489 000 million in the same period of 1969. However, at the same time *official gold and foreign exchange reserves* went down by Lit. 179 000 million, in other words by more than the deficit, since the banks began once again to export capital, as they had not done the year before. At the end of October reserves totalled Lit. 2 979 000 million.

From December 1969 to August 1970 the banks' *domestic liquidity* continued to shrink appreciably, but it should have started increasing again from the middle of the year as a result of a certain relaxation of monetary and credit policy by the authorities. A very strong boost to greater liquidity came from Treasury operations, as the capital market had dried up and there was a temporary delay in tax receipts and an accumulation of expenditure owing to strikes by public employees. In the first nine



months expenditure was over 21% higher than a year earlier, though capital spending had declined. These factors were, however, outweighed by those exerting a restrictive effect on liquidity, i.e. payment transactions with abroad, an exceptionally fast increase in the circulation of banknotes and the Banca d'Italia's refinancing operations. The cost of these operations has been raised by the monetary authorities several times since March 1969.

Bank customers' deposits grew more slowly and at the same time there was a distinct shift from savings to sight deposits. During most of the year *bank advances* also grew somewhat more slowly; in the first eight months they were 13.8% higher than a year earlier (in the first quarter 14.3%).

The growth of the circulation of banknotes and the switch in deposits brought about an accelerated and extraordinarily fast growth of *the supply of money*[1]: 11.7% from December 1969 to September 1970, compared with 4.9% a year earlier. In September the supply of money was 23% larger than in September 1969.

On the *securities market* bond prices continued to decline in the first half of the year, and from May share prices likewise tended to go down, at any rate until early November. The weakness of bond prices was probably due to the worldwide increase in interest rates, the wait-and-see attitude of savers and a general increase in their preference for cash. The cautious attitude of savers no doubt reflected the fact that investment in fixed-interest securities is now also fraught with greater uncertainty since the Banca d'Italia largely gave up its price support policy in the first half of 1969. The net volume of bonds issued on the Italian capital market in the first eight months of 1970 was nearly 50% less than in the same period of 1969. Owing to the barrenness of the Italian capital market the lively growing demand for capital was increasingly met by recourse to abroad, as has already been mentioned.

Consequently, the level of interest rates rose considerably in 1970. The yield on bonds increased by over 2 points to 9.4% during the first seven months, but then it tended once again to decline slightly.

1 According to the Banca d'Italia's definition (notes and coin, customers' current accounts, and bank drafts, i.e. the "vaglia cambiari" issued by certain banks and "assegni circolari").

Demand for and supply of goods and services

	1968 [1]	1969 [1]		1970 [2]		1971 [3]
	At current prices (in Lit '000 million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports [4]	9 119	+ 14.1	+ 15.6	+ 9	+ 13½	+ 11
Gross fixed asset formation	9 165	+ 8.2	+ 15.0	+ 7½	+ 18½	+ 5
Public current expenditure on goods and services	6 363	+ 3.1	+ 8.1	+ 4	+ 10	+ 6
Private consumers' expenditure	29 995	+ 5.7	+ 8.8	+ 9	+ 14½	+ 7
Gross national product	47 134	+ 5.0	+ 9.2	+ 6½	+ 13½	+ 6
Imports [4]	7 698	+ 20.7	+ 21.3	+ 19½	+ 23	+ 14½

[1] "Relazione generale sulla situazione economica del Paese (1969)".
[2] Commission estimates.
[3] Commission forecasts.
[4] Goods, services and factor income.

Note :

(a) The difference between the figures for demand and those for supply is accounted for by movements in stocks.
(b) The estimates and forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with experts from the member countries, but are established and published on the sole responsibility of the Commission.

2. Outlook for 1971

Despite certain restraining influences, an overall lively expansion of production and employment seems very possible for 1971, largely because of the latest government measures. This expansion depends to a great extent, however, on a return to normal in relations between the two sides of industry, which is also of decisive importance for the re-establishment of general economic equilibrium. Such a return to normal has been expressly assumed in this Chapter; if relations between employers and workers do not move in this direction, the prospects outlined below will not be realized.

Subject to this reservation a rapid expansion of *demand for exports* can be expected, especially visible exports, for which there will continue to be considerable potential demand in the member countries. Once the international competitiveness of Italian suppliers has been restored through shorter and more reliable delivery dates, this demand will doubtless become effective. The expected slackening of the world business trend will certainly be more than offset by such a development. The new customs tariff reductions, which are to be put into effect by numerous non-member countries on 1 January 1971 in accordance with agreements concluded during the Kennedy Round, will likewise encourage Italian visible exports. Exports of services are also expected to increase vigorously.

All in all, *domestic demand* may well expand appreciably too; towards the end of the year, purchases to beat value added tax may play a certain role here as the date of its introduction approaches.

As a whole capital expenditure will expand vigorously. In *building and construction,* however, a persistence of the declining trend of investment observed in 1970 must be expected. For, although public works may increase considerably because of very extensive current and planned programmes, and a tendency towards stabilization in the building and construction sector may grandually set in, residential construction is likely to slow down further and thus depress the level of total expenditure on building.

A sharp growth of investment in *plant and machinery* is suggested by numerous points—namely, the expected improvement in the psychological climate through the re-establishment of peace on the labour front and the Government's energetic economic steps; the—on the whole very expansionary—outlook for demand and its favourable effects on the situation of business firms' profitability, which is at present severely strained; the increased supply of credit as a result of measures put into effect in August and September; the tax incentives to investment introduced at the same time; the urgent need for rationalization to counterbalance the rapid upsurge of labour costs and to improve competitiveness; and in some industries the need to expand technical productive capacity.

Investments in *stocks* are again likely to increase sharply as a result mainly of further progress towards the normal in respect of stocks of raw materials and finished goods.

What may be predicted with greatest certainty is that there will be a renewed vigorous expansion of *consumer spending,* in particular by private consumers. Firstly, households' propensity to save may decline further with the easing of labour relations and as a result of the appreciable rise in prices over several years, especially since the reduction in expenditure on residential construction may tend to increase the percentage of households' income available for consumer spending. Secondly, it is expected that the growth of such income, albeit slower than before, will still continue rapidly, as the number of employed persons and, more particularly, per capita wages and salaries may well increase vigorously. An appreciable growth of other forms of income is also expected.

On the basis of these assumptions regarding demand, and of the probable widening of the margin of available capital, there is likely to be a good 8% increase in *industrial production* and a 6% growth of real *gross national product.*

Although, with the anticipated return to normal of the process of production, the growth rates of demand and domestic supply may be nearer to each other than in 1970, *imports* will probably increase very vigorously in 1971 too, and somewhat faster than exports. In this case the *balance of exports less imports* (as defined for national accounts) would again shrink, though to a relatively small degree.

The *price* level will in all probability continue to mount rapidly. It is likely that the rise in costs, which was exceptionally sharp in 1970, will be passed on to prices more and more in a situation where demand is growing briskly. In addition, there are further factors pushing up costs and prices: the imminent renewal of collective wage agreements, in which the wage increases made recently cannot but provide a standard for comparison and thus play an important role; the reductions in working hours already agreed on for 1971; non-contractual wage adjustments and the raising from 1 January 1971 of social charges to be paid by firms and in August 1970 of numerous indirect taxes.

In view of these prospects and of the introduction of the value-added tax system by 1 January 1972 at the latest, *short-term economic policy* should give priority to reducing as far as possible the strains in the demand/supply relationship, which are likely to persist, albeit with reduced intensity, even after restoration of peace on the labour front. Measures taken here should avoid exerting too strong an influence on the propensity to invest.

The action taken at the end of August by the Government—the details are given in the section "Major economic policy measures"— represents an energetic and important step towards restoration of the conditions for a balanced expansion of the economy.

Budgetary policy, which should play the main role, must be aimed at keeping the expansion of public expenditure down to the indispensable minimum. The budget estimates for 1971, in which the increase in expenditure is, at just under 11%, below the likely increase in gross national product in money terms (see "Major economic policy measures"), would seem to be aimed in this direction; when the money comes to be paid out, there may still be margins which could be used to check excessive growth. In the first half of the year, in particular, the growth of expenditure ought to be even less than the rate proposed in the budget estimates. Within total public expenditure, capital spending should increase faster than other expenditure; however, despite the needs of urgent infrastructure projects, any increases should be made gradually, not abruptly.

From the angle of public revenue a reform of the tax system seems to be increasingly desirable for both structural and short-term economic reasons; such a reform would have to enable the tax base to be widened in a manner acceptable from the social angle. For the time being there should be no further raising of indirect taxes or increase in public service charges, because of their effects on costs and prices. The remaining cash deficit, which must be reduced as far as possible, should be financed not by monetary means but directly by real saving.

A restraining line of monetary and credit policy seems required until overall economic balance has been achieved. In particular it would be impossible to curb the expansion of credit if, despite the latest increases in taxes and social contributions, which tend to reduce the public authorities' need for credit, it threatened to exceed the limit compatible with balanced economic expansion. In such a case, care should be taken to spare, as far as possible, those credits which help to finance investments that are productive relatively fast. However, it would seem advisable at all events to limit the growth of consumer-oriented credit. A sharp decrease in interest rates would probably not be advisable at present, for balance of payments reasons among others.

The main objectives of capital market policy should be to increase domestic supply of capital and make it help as effectively as possible in covering the long-term financing requirements of commerce and industry and the public authorities, which are particularly great in Italy. A point worth mentioning in this connection is the encouragement of saving for building purposes by means of government premiums, especially as this could clearly have beneficial effects from the angle not only of short-term economic policy but also of structural and social policy. Furthermore, consideration could be given to whether saving by households should not be encouraged in a general way by granting premiums. These and other similar incentives to save (e.g. tax incentives) would yield results all the faster according to the extent to which the price trend could be stabilized. Efforts to increase the number of Italian shares quoted on the stock exchange and plans to introduce Italian investment funds would probably also serve to meet the above objectives.

In conclusion, it must be stressed that re-establishment and consolidation of the basis for rapid and sustained economic growth in the medium term as well as the short term cannot be achieved if the behaviour of all those concerned in the process of production fails to take into account the need to increase productivity and to stabilize costs and prices.

Major economic policy measures

May

Enactment of a law on the setting-up of the "ordinary statute" regions. The main points are: yearly expenditure (according to rough estimates Lit. 700 000 million, equal to 3½% of total public expenditure in 1969), which is only in part offset by reduced expenditure in the rest of the public sector, is to be financed by the region's own taxes (road tax and other indirect taxes yielding some Lit. 90 000 million) and by a share of certain central government taxes *(amounting to about Lit. 610 000 million). Other funds will flow into the regions from government subsidies, from a government regional development fund and from loans (exclusively for investments and acquisition of holdings) and advances (only for temporary cash needs). Debt servicing may not exceed 20% of tax receipts. The transfer to the regions, as required by the Constitution, of responsibilities which have hitherto belonged to the central government is to be implemented by decrees to be issued within the next two years.*

July

At the end of the month submission of the budget estimates for 1971: income, excluding proceeds from loans floated, 11.1% higher (in the 1970 budget 12.5%); expenditure excluding redemption of debts up 10.9% (15.1%); deficit Lit. 1 559 000 million (Lit. 1 422 000 million). Further distinct increase in the current account's share of total budget spending, but decrease of government expenditure to be financed initially outside the budget (from Lit. 1 194 000 million to Lit. 877 000 million). This estimate of tax receipts is based mainly on the assumption that real GNP will go up in 1971 by 5% and prices by 4.8%.

August

At the end of August the new Government's decree law with important short-term economic measures to restore economic equilibrium and to reorganize the distribution of resources so as to encourage productive investments and social spending and check private consumers' expenditure: absorption of households' purchasing power by increasing numerous indirect taxes on luxury and semi-luxury goods and services (in particular an increase of around 15% on petrol, special tax on tolls levied by motorway concession holders, 8 to 30% increase in turnover tax rates for certain luxury goods) and some charges (for example the increase in stamp duty) and by raising withholding tax (from 1.5 to 4%), with effect from 1 January, on earned income of over Lit. 5 million per year. Imposition of a 7.5% tax on the sale of luxury dwellings and of land intended for the construction of such dwellings. Additional tax income from these measures estimated at about Lit. 450 000 million per year, of which some Lit. 130 000 million already in the last four months of 1970. This sum goes into a special Treasury account; it is to be used to reduce the deficit of health insurance funds and for the planned restructuring of the public health system. Raising of refund on medicine allowed to health funds (to 25%, 19% of which to be borne by the manufacturers and the rest by the chemists). On the other hand, production and investment incentives through credit and taxation measures, in particular: increase of the endowment capital of some special credit institutions (especially Mediocredito: *by Lit. 170 000 million within three years), which deal in particular with the medium-term financing of small and medium-sized firms; raising of interest rebates for advances to such firms; extension in range or time of tax relief on yield from the sale of land or securities if reinvested in plant and machinery, and on mergers and industrial investments in firms which, in the current and following two financial years, exceed their average level for the preceding five years. Tax incentives for having shares quoted on the stock exchange, for increases of capital and issues of loans in the form of convertible bonds by companies with shares quoted on the stock exchange, and for borrowing abroad by Italian firms. From 1 January 1971, increase in employers' social security contributions (by an estimated Lit. 230 000 million per annum or 1.5% of the total wages and salaries bill); this additional sum is also to be used for the restructuring of the public health system.*

September

In the midle of the month, easing of minimum reserve rules with effect from 1 October in order to increase the credit potential of the special credit institutions, on which small and medium-sized undertakings largely depend for their financing. Raising from 3.75 to 5.5% of the rate of interest on the banks' minimum reserves held in liquid funds or Treasury bills. In view of current credit policy requirements the Banca d'Italia will allow banks to include in their minimum reserves bonds issued by property credit institutions in place of liquid funds and Treasury bills. Up to the end of 1970 the commercial banks may acquire bonds to the value of about Lit. 250 000 million; the sum corresponds to around 1% of the value of customers' deposits with these banks.

October

Towards the end of the month, publication of a law which introduces a number of tax measures with social policy aims as from 1 January 1971: increases in certain tax-free allowances (especially for wage and salary earners), reductions in rates of taxation for lower incomes, wider application and raising of tax deducted at source on income from self-employed activities, raising of the 10% special supplement on income tax rates, introduced in autumn 1966, to 15%. The tax relief and additional tax burdens resulting from these measures (each about Lit. 160 000 million for the year) are to cancel each other out.

Likewise at the end of the month: as the two months' deadline for converting the decree issued in August into a law was not met, the Government issued a new decree law, which essentially embodies the same short-term economic measures as the August one (see above) and which in its turn must be adopted as a law before the end of the year. By comparison with the original decree law, the main changes are as follows: some reductions in the additional tax burdens (e.g. the increase in turnover tax on certain luxury goods now ranges from 7 to 20%), further raising of endowment capital, extension until the end of 1973 of current rent control provisions and of certain long-term tax exemptions for the construction of new buildings, authorization to motorway concession holders to increase tolls so that their additional tax burden may be passed on to motorists.

TABLE 1 : **Key indicators**

	1965	1966	1967	1968	1969	1969
	% change by volume on preceding year					1958=100
Gross national product	3.6	5.9	6.4	6.0	5.0	134
Industrial production	3.3	7.4	8.7	8.7	5.2	140
Total imports	1.9	13.7	12.6	7.5	20.7	161
Private consumers' expenditure	2.7	6.8	7.3	4.7	5.7	134
Public current expenditure on goods and services	3.6	3.2	2.8	4.1	3.1	123
Gross fixed asset formation	– 8.7	4.0	10.5	7.7	8.2	115
Total exports	20.1	13.2	6.2	15.4	14.1	212
Gross national product per head of population	2.5	5.1	6.0	5.4	4.3	126
Gross national product per person in employment	5.5	7.4	5.4	6.1	6.0	138
	% change by value on preceding year					
Gross income per employee	8.1	7.9	8.0	7.2	7.5	165

TABLE 2 : **Indicators for internal and external equilibrium**

	1965	1966	1967	1968	1969
Balance exports less imports					
in million u.a.	1 867	1 723	1 235	2 274	1 930
as percentage of GNP	3.3	2.7	1.8	3.0	2.3
Unemployment rate	3.6	3.9	3.5	3.5	3.4
price index of private consumers' expenditure (% change on preceding year)	4.1	2.9	2.9	1.5	2.9

TABLE 3 : Foreign trade (at current prices)

	% change on preceding year					1963 = 100	Million u.a.	% of totals
	1965	1966	1967	1968	1969	1969	1969	1969
Visible exports								
Total	20.7	11.7	8.3	17.0	15.3	233	11 736	100.0
Intra-EEC	27.6	12.8	3.3	20.9	22.2	278	4 986	42.5
To non-EEC countries	16.4	11.0	11.6	14.5	10.6	188	6 750	57.5
Exports of food, beverages and tobacco								
Total	20.5	1.5	4.7	− 3.7	15.7	146	1 006	8.6
Intra-EEC	31.4	0.4	− 1.7	− 1.3	21.4	169	550	4.7
To non-EEC countries	9.5	2.8	12.4	− 6.1	9.5	126	456	3.9
Exports of raw materials, fuel and power								
Total	18.7	10.6	9.1	14.1	1.1	189	895	7.6
Intra-EEC	34.2	21.5	15.9	14.7	− 2.0	262	334	2.8
To non-EEC countries	12.4	5.2	5.3	13.7	3.1	162	561	4.8
Exports of semi-finished and finished industrial goods								
Total	20.9	13.4	8.8	20.2	16.7	253	9 835	83.8
Intra-EEC	26.2	14.6	3.2	25.4	24.9	306	4 101	35.0
To non-EEC countries	17.8	12.6	12.4	16.7	11.5	225	5 734	48.8
Visible imports								
Total	1.6	16.7	12.9	4.3	21.5	165	12 453	100.0
Intra-EEC	− 3.1	21.6	21.5	9.1	29.9	195	4 819	38.7
From non-EEC countries	3.9	14.4	8.8	1.8	16.7	151	7 634	61.3
Imports of food, beverages and tobacco								
Total	18.9	9.7	0.7	8.5	14.9	167	2 118	17.8
Intra-EEC	20.6	13.5	26.6	29.0	26.8	328	789	6.3
From non-EEC countries	18.4	8.7	− 6.4	0.9	9.2	132	1 429	11.5
Imports of raw materials, fuel and power								
Total	8.5	15.1	13.7	1.0	13.0	161	4 170	33.5
Intra-EEC	18.7	18.2	14.2	− 3.0	20.6	187	597	4.8
From non-EEC countries	7.0	14.6	13.6	1.7	11.8	157	3 573	28.7
Imports of semi-finished and finished industrial goods								
Total	− 10.8	22.0	18.8	8.6	31.0	167	6 064	48.7
Intra-EEC	− 10.8	24.2	22.3	8.1	32.4	179	3 432	27.6
From non-EEC countries	− 10.9	19.4	14.5	9.2	29.1	154	2 632	21.1

TABLE 4 : Selected monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1963 = 100)	1968	136.3	127.5	136.7	133.7	135.0	138.2	137.3	138.7	142.3	141.9	136.8	144.4
	1969	146.1	143.9	147.3	147.7	145.0	151.6	150.0	136.2	137.7	127.5	126.4	133.3
	1970	152.8	154.2	153.6	150.8	148.2	150.7	152.0	138.9	(159.0)			
Unemployed (1 000)	1968	970.4	963.8	952.7	943.7	962.1	958.2	962.3	962.9	975.3	976.6	952.1	931.3
	1969	933.8	938.7	915.3	895.8	883.0	896.6	883.3	875.3	879.5	868.4	844.7	827.8
	1970	845.7	841.8	846.3	846.2	851.5	864.7	879.5	891.2				
Construction : permits for residential construction (1 000)	1968	31.3	48.1	55.3	55.6	53.6	60.5	69.0	313.4	78.6	72.7	38.6	45.6
	1969	19.4	21.4	23.3	21.4	25.3	22.8	25.1	22.6	25.8	25.3	24.5	24.4
	1970	17.0	22.3	24.6	25.3	27.5	24.8						
Private consumers' expenditure : department store turnover (1963 = 100)	1968	137.9	150.3	146.8	154.1	149.7	149.6	159.5	159.9	152.2	155.0	161.1	156.7
	1969	155.1	150.6	164.4	159.7	182.0	162.7	174.6	183.1	183.2	172.9	169.1	177.5
	1970	183.1	179.7	199.2	170.9	170.2	(195.0)						
Consumer prices (1963 = 100)	1968	118.7	118.7	118.8	119.0	119.1	119.0	118.8	118.8	118.9	119.0	119.2	119.6
	1969	119.9	120.1	120.6	121.1	121.4	121.8	123.1	122.9	123.1	123.4	124.1	124.6
	1970	125.1	126.1	126.6	127.2	127.7	128.0	128.2	128.4	129.2			
Visible imports (million u.a.)	1968	713.0	734.5	826.1	844.9	876.2	850.4	860.1	903.3	910.1	778.9	1 013.6	946.5
	1969	972.3	940.1	934.1	995.7	1 046.7	1 078.2	1 093.5	1 071.0	1 108.8	1 008.8	1 111.8	1 114.3
	1970	1 174.4	1 058.5	1 142.9	1 250.8	1 252.7	1 320.3	1 311.1	1 295.0				
Visible exports (million u.a.)	1968	796.5	794.0	800.9	820.1	843.2	829.4	846.6	842.4	822.7	870.0	1 002.5	907.5
	1969	937.0	935.5	912.7	1 025.1	1 075.8	1 008.6	1 086.8	922.1	995.7	913.6	1 007.6	860.4
	1970	1 080.9	949.9	965.0	1 118.4	1 113.3	1 155.6	1 121.5	1 141.5				
Balance of trade (million u.a.)	1968	+ 83.5	+ 59.5	− 25.2	− 24.8	− 33.0	− 21.0	− 13.5	− 60.9	− 87.4	+ 91.1	− 11.1	− 39.0
	1969	− 35.3	− 4.6	− 21.4	+ 29.4	+ 29.1	− 69.6	− 6.7	− 148.9	− 113.1	− 95.2	− 104.2	− 253.9
	1970	− 93.5	− 108.6	− 177.9	− 132.4	− 139.4	− 164.7	− 189.6	− 153.5				
Official gold and foreign exchange reserves (net million u.a.)	1968	5 139	5 150	5 105	5 082	5 042	5 086	5 141	5 270	5 188	5 195	5 069	4 878
	1969	4 727	4 636	4 493	4 571	4 366	4 514	4 582	4 686	4 547	4 566	4 668	4 696
	1970	4 457	3 943	3 947	3 923	4 368	4 233	4 130	4 226	4 411	(4 767)		
Money supply (Lit. '000 million)	1968	17 863	17 652	17 976	18 235	18 463	18 795	18 993	18 975	19 379	19 373	19 695	21 104
	1969	20 440	20 379	20 836	20 845	21 282	21 558	21 590	21 681	22 138	22 351	22 831	24 388
	1970	23 839	24 122	24 689	24 896	25 538	26 117	26 522	26 660	27 232			

NOTES TO GRAPHS AND TABLES

Source : Statistical Office of the European Communities (except as otherwise indicated).
Conversion into units of account (1 u.a. = 0.888671 g of fine gold = US $ 1) at official exchange rates.

Graph 1

— Exports fob : series adjusted for seasonal variations; three-month moving averages.

Graph 2

— Industrial production (excluding construction, food, beverages and tobacco) : indices adjusted for seasonal variations; three months moving averages.

Graph 3

— Labour market : number of registered unemployed; series prepared by the Ministero del Lavoro e della Previdenza Sociale and adjusted for seasonal variations by the Statistical Office of the European Communities; three-month moving averages.

Graph 4

— Imports cif : series adjusted for seasonal variations; three-month moving averages.

Graph 5

— Wages and consumer prices : source ISTAT. Agreed minimum wages in industry (excl. family allowances).

Graph 6

— Merchandise trade balance : difference between the figures for seasonally adjusted exports and seasonally adjusted imports.

Graph 7

— Bank lending to commerce and industry : source Banca d'Italia. Short-term loans to business and private consumers; position at end of month.

Table 1

Source for 1968 and 1969 : Relazione generale sulla situazione economica del Paese (1969).

— GNP at market prices.
— Industrial production : value added by industry at factor cost.
— Total exports and imports : goods, services and factor income.
— Gross income per employee : income from paid employment (not including social insurance contributions borne by the State).

Table 2

— Net exports : goods, services and factor income.
— Unemployment rate : number of unemployed as percentage of labour force (annual average); Source ISTAT.
— Price index : implicit price index for private consumption, computed from the national accounts.

Table 3

— Exports fob, imports cif; the products have been regrouped on the basis of the Statistical and Tariff Classification for International Trade (CST) : food, beverages and tobacco (Groups 0 and 1 CST), raw materials, fuel and power (Groups 2-4 CST), semi-finished and finished industrial goods (Groups 5-9 CST).

Table 4

— Industrial production : adjusted for seasonal variations, excluding construction, food, beverages and tobacco.
— Unemployed : series provided by the Ministero del Lavoro e della Previdenza Sociale, adjusted for seasonal variations by the Statistical Office of the European Communities.
— Construction : dwellings authorized in the provincial capitals and in other communes with more than 20 000 inhabitants; figures not seasonally adjusted.
— Private consumers' expenditure : value index of department store turnovers, adjusted for seasonal variations.
— Consumer prices : unadjusted index.
— Imports cif, exports fob; adjusted for seasonal variations.
— Balance of trade; difference between seasonally adjusted exports and imports.
— Official gold and foreign exchange reserves (net); source Ufficio Italiano dei Cambi; position at end of month.
— Money supply : notes and coin in circulation excluding cash holdings of the Treasury. Sight deposits of non-banking sector with credit institutions, bank drafts in circulation (whether *vaglia* or *assegni*) issued by the Banca d'Italia and other banks and credit institutions; position at end of month.

D. Netherlands

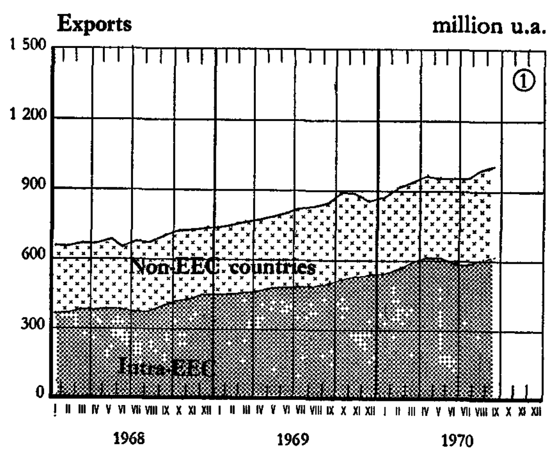
The social unrest which broke out in the Netherlands in the summer, and the resulting upward surge of wages, have very clearly demonstrated the implications for the internal and external equilibrium of the Dutch economy of the economic overheating caused by increasing excess demand. The expansion of exports has lost momentum since the beginning of 1970 but that of consumer demand and investment by enterprises has quickened, leading to an extremely high degree of technical capacity utilization and a serious labour shortage. The very sharp increase in imports, mainly attributable to the reduced elasticity of domestic supply, has caused the balance of exports less imports to deteriorate considerably. Concurrently, there have been marked upward pressures on prices.

The vigorous increase in costs and prices will continue to affect the trend of economic activity fairly well into 1971. The spontaneous growth of demand indicates that overheating is likely to persist, rather than otherwise—especially as there will probably be little room to expand production, despite the considerable investment of previous years. Re-establishment of satisfactory internal stability, which is also a prerequisite for better external economic balance, should therefore be a priority aim of economic policy.

1. Balance sheet for 1970

The year 1970 was marked by increased strains in the Dutch economy. The extremely high level of technical capacity utilization, and the reduction in hours of work, had the effect, in particular, of preventing domestic supply from keeping pace with the unusually rapid growth of demand. The pull exerted by demand, which was more and more in evidence in the course of the year, therefore not only led to a rapid increase in imports and a strong deterioration in current account but was also associated with unrest on the labour front and additional wage rises. This pattern induced the Dutch authorities to direct economic policy more towards the elimination of excess demand.

Exports showed a further strong increase in 1970, parallel with the continuing rapid growth of international trade. The competitive position of the Dutch economy remained favourable, at least to judge by the relatively slight rise in wage costs up to the autumn. Nevertheless, the substantial impact of domestic demand, reinforced by the slackening inflow of orders from abroad, led to a somewhat slower increase of visible exports in the course of the year. On the basis of customs returns, the increase in their value as a whole at current prices in 1970 can be estimated at more than 18%, as against 19.5% in 1969. The slight year-to-year slackening of deliveries to the other Member States was



mainly attributable to the very hesitant trend of French demand, which was not fully offset by increasing exports to the other Member States, more particularly to Germany. Similarly, exports to non-member countries did not rise quite so much as in 1969.

Receipts from services and factor income from abroad climbed somewhat more steeply, so that total exports in 1970 will have increased at about the same rate as in 1969 (17.5%).

The growth of domestic expenditure made an increasing contribution to the economic upturn. An important element of this growth was the appreciably quicker rise of fixed investments. Major incentives to invest were the strong pull exerted by demand, the pressure to rationalize and modernize, and the still quite large possibilities open to firms for self-financing—swelled by refund of the previously collected turnover tax on stocks. Furthermore, the substantially higher level of private capital imports cushioned the impact of the restrictive credit policy on bank loans to firms.

A completely different picture was presented by residential building, which was appreciably inhibited by the manpower shortage, high interest rates and the marked upward surge of building costs and therefore, as in the previous year, attracted less investment in real terms. Public capital expenditure increased more quickly in terms of value than in 1969, but the increase at constant prices was very moderate because of the rise in building prices.

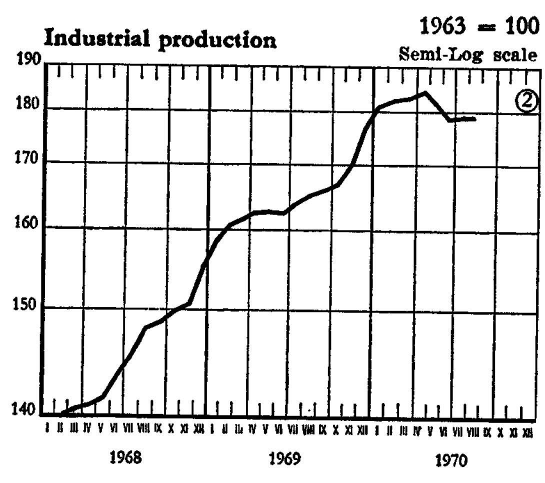
Overall, gross fixed asset formation at current prices probably increased by about 15% as against 7.9% in 1969. But the overall rise in the prices of capital goods was still greater than the very high rate recorded in the previous year.

Economic activity was strongly boosted by stockbuilding in 1970. Nevertheless, entrepreneurs seem to have adopted a more cautious policy here in the second half of the year, as a result of the decline in raw material prices and the continuing high level of interest rates.

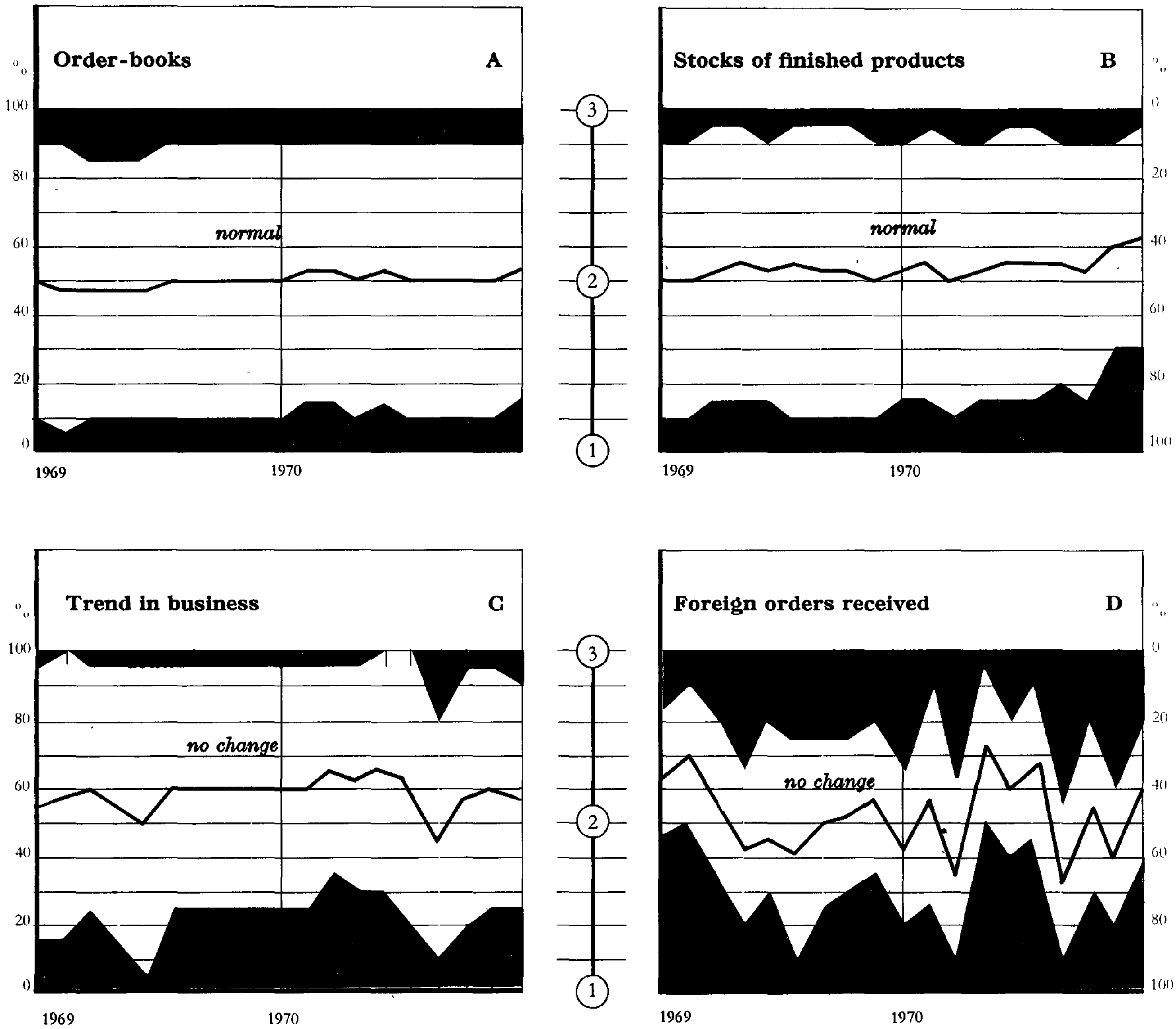
The consumption boom was more and more marked during 1970. Public current expenditure, for instance, seems to have risen more strongly than in the previous year. Not only did civil service salaries follow the general trend of wages in the private sector, as usual, but the State also made extensive purchases of goods and services, especially for defence.

The faster rise of private consumers' expenditure also exerted increasing pressure on available resources. Contrary to what had been expected, the increase in the wage bill did not in fact slow down in 1970. The increase in wages per employed person can be put at about 12.5% as against more than 11% in 1969, mainly owing to the additional wage rises conceded after August and a bigger wage drift than in the previous year. The buying power of wage earners increased more in 1970 than in any year since 1964, thanks to the fact that the consumer price index rose more slowly than in 1969 and to the partial offsetting of the progressively heavier incidence of graduated taxes by the introduction of the first stage of the wage and income tax reduction (designed to neutralize the erosion of taxable incomes by inflation in the period from 1968 to 1971). Transfer incomes showed a similar trend, more particularly because of the structural improvements of pensions and family allowances introduced in 1970. Allowing for a slight decline in the propensity to save, private consumers' expenditure probably increased by about 12.5 % in 1970 as against 10.5% in 1969 at current prices, and probably by some 8% as against 4% in 1969 at constant prices.

Despite its reduced elasticity, aggregate domestic supply increased at a higher annual rate than in 1969. Industrial production was an exception —in 1970 its contribution to the gross national product at constant prices was up by 10% on 1969, that is to say, growth was much the same as in the previous year. In terms of the trend, its rate of growth has slowed markedly since



BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Source : Business survey of the Centraal Bureau voor de Statistiek.

Note : The survey includes construction but not paper, petroleum, non-metallic minerals.

GRAPHS A, B, C and D : The three colours (green, yellow and red) show the percentages of the three different answers.

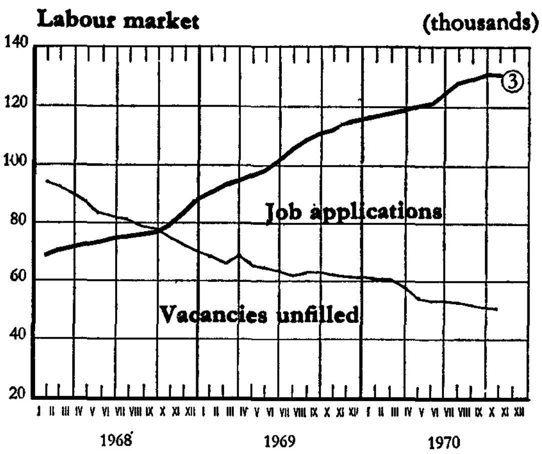
The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows :

by 0.03 for the answer "above normal", or "up";
by 0.02 for the answer "normal", or "no change";
by 0.01 for the answer "below normal", or "down".

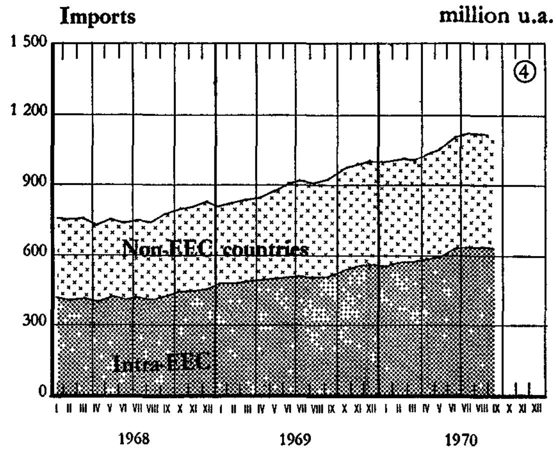
the first quarter of 1970. The revival of demand for industrial and commercial buildings pushed up production in building and construction, but to a limited extent, owing to the particularly marked manpower shortage in this sector and the fact that labour productivity increased only slightly. The livelier growth of consumer expenditure may have decisively contributed towards the expected more rapid increase in output in the services sector. It may well be that agricultural production also increased faster in 1970.

The gross national product at constant prices will probably turn out to have grown almost 6% in 1970 as a whole, compared with 5.1% in 1969.

Strains increased on the labour market in 1970. Skilled labour in the western parts of the country, in particular, constituted serious bottlenecks. The seasonally adjusted number of unfilled vacancies rose steadily, despite the considerable expansion of the domestic labour force and the increasing influx of foreign workers, while unemployment fell to its lowest level since 1966—the unemployment rate (percentage of unemployed, seasonally adjusted, in the total civilian labour force) was only 0.5% in September, as against 1.4% in the same month of the previous year. Concurrently, the number of vacancies rose to more than two and a half for every person out of work.

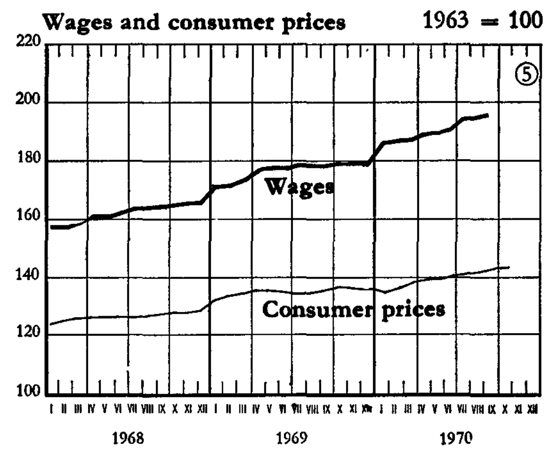


The increasing difficulties met by domestic enterprises in their endeavours to meet soaring demand led to a rapid rise in imports, more especially from April onwards. This trend particularly affected capital goods, and to a lesser extent consumer durables. The upshot was that visible imports, at constant prices, rose at an annual rate of 14%, only slightly less than in 1969. Assuming a relatively high increase in expenditure on services and in factor income,



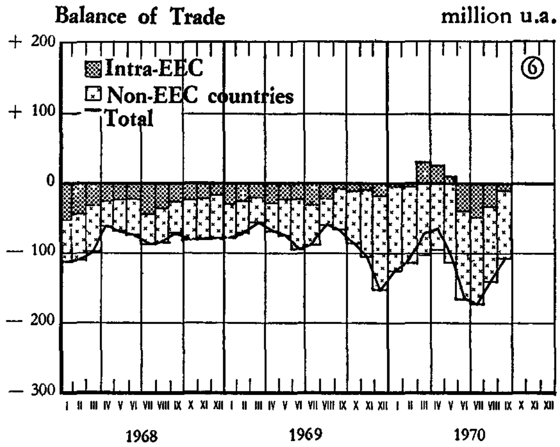
aggregate imports in 1970 may well have shown a year-to-year increase of 14% as against close on 14.5% in 1969 (constant prices). However, import prices probably rose much more quickly in 1970 than in 1969, despite the lull in the second half of the year.

The price climate again deteriorated markedly in 1970, with capital goods recording particularly high price increases. The soaring import prices for capital goods and the upward thrust of building costs, particularly the latter, led to a price jump of about 9% in this sector by the end of the year. The upward trend of consumer prices steepened distinctly in the course of the year



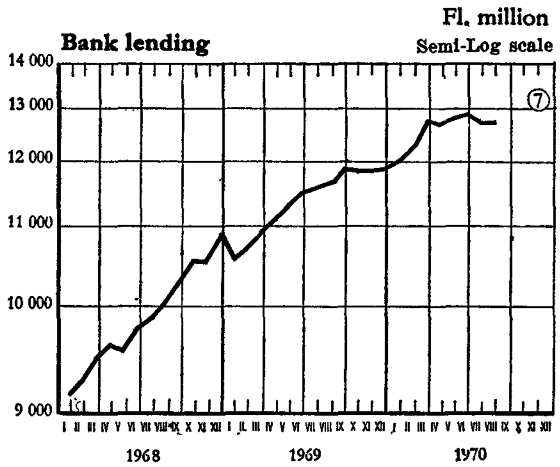
—firstly because the price policy was temporarily relaxed half way through 1970 and certain autonomous factors making for higher prices, such as rent increases, had an impact, and secondly because the sharp increase in import prices and also, after the end of the summer, the greater wage cost pressure, probably exerted an influence. The consumer price index climbed 5.3% between December 1969 and September 1970.

The lower coverage rate resulting from the faster advance of imports and the slower increase of exports led to a very large trade deficit, even though the tendency for the terms of trade to deteriorate did not persist. Services and factor



income contributed higher net earnings, but the balance on current account on the basis of transactions for the period from January to August closed with a deficit of Fl. 858 million, or about Fl. 500 million more than in the corresponding period of 1969. On the other hand, the net inflow of private long-term capital (close on Fl. 1 600 million in the first eight months of 1970) far exceeded the net outflow of short-term capital, so that capital transactions yielded a substantial surplus. The result was that the overall balance of payments for the period from January to August closed with a surplus of Fl. 748 million. The net gold and foreign exchange reserves of the Central Bank (including the position with the IMF) rose by Fl. 1 182 million over the same period, while the commercial banks' foreign exchange went down by Fl. 434 million.

The sharp increase in liquidity resulting from transactions with abroad contrasted with the weaker stimulus to domestic liquidity from public monetary financing, which contracted somewhat. The deficit on the Central Government's budget may have been somewhat smaller than in 1969, even though public spending again showed a substantial increase (in the first eight months of 1970 it was 13.9% up on the corresponding period of the previous year). The deficit was probably covered almost exclusively by non-monetary means. The money supply (notes and coin in circulation and sight deposits) nevertheless rose more than Fl. 2 200 million between January and August, i.e. 12% more than in 1969, owing to monetary financing by local authorities and the fact that private-sector transactions with the bank system made a much bigger contribution to expansion than in 1969. Short-term bank lending to the private sector between March and October exceeded the credit ceiling limits. In early September these limits were set, for the period from September to the end of December 1970, at 3.5% of average lendings in the last quarter of 1969;



this represented a reduction in the admissible maximum rate for the year as a whole from 10% in 1969 to 9.5% in 1970. Allowing for the perceptible increase in medium-term loans, total bank lending to the private sector was about 18.5% higher in August than in August 1969.

Fairly severe strains persisted on the capital market. Public recourse to the capital market hardly changed, but calls by firms showed a further increase, so that the aggregate total of loans floated was higher than in 1969. The trend of long-term interest rates pointed upwards till the beginning of the summer, and then declined slightly, mainly owing to the inflow of foreign capital attracted in particular by the relatively higher interest rates obtaining in the Netherlands.

Demand for and supply of goods and services

	1968 [1]	1969 [1]		1970 [2]		1971 [3]
	At current prices (in Fl. '000 million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports [4]	42.06	+ 15.6	+ 17.5	+ 13	+ 17½	+ 9½
Gross fixed asset formation	24.18	+ 0.6	+ 7.9	+ 5½	+ 15	+ 5
Public current expenditure on goods and services	14.33	+ 1.7	+ 11.8	+ 4	+ 14	+ 1½
Private consumers' expenditure	51.67	+ 4.0	+ 10.5	+ 8	+ 12½	+ 5
Gross national product	91.87	+ 5.1	+ 11.4	+ 6	+ 11½	+ 4
Imports [4]	41.47	+ 14.5	+ 18.4	+ 14	+ 20½	+ 9½

[1] Statistical Office of the European Communities.
[2] Commission estimates.
[3] Commission forecasts.
[4] Goods, services and factor income.

Note:
(*a*) The difference between the figures for demand and those for supply is accounted for by movements in stocks.
(*b*) The estimates and forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with the experts of the member countries but are established and published on the sole responsibility of the Commission.

2. Outlook for 1971

The economic prospects for 1971 in the Netherlands are still fraught with uncertainties. Domestic supply will probably remain subject to severe strains to begin with, and a fairly high deficit will be recorded on current account, even if the short-term economic policy programme—including a temporary wage freeze—announced by the Government can be fully implemented.

Exports, however, will give a markedly weaker fillip to economic growth. The main factor here will be the expected slackening of demand from EEC Member States, especially Germany and Belgium. But deliveries to non-member States are also likely to lose momentum, despite the probable upturn of the American economy and the new series of tariff reductions agreed at the Kennedy Round in GATT. Another major factor behind the slower growth of exports, at least in the first half of the year, will be the inadequate supply potential. Here, the possibility of gradually releasing capacity for export again will depend mainly on whether the restrictive measures succeed in checking the growth of domestic demand. Apart from this, export prices are likely to rise more slowly than in 1970, although Dutch wage costs may increase faster than elsewhere. Competition on export markets will, in fact, probably be substantially keener than in 1970, and make it more difficult to pass wage costs on to export prices. These prospects suggest that exports of goods and services (as defined for the national accounts) will increase by about 10½% as against 17½% in 1970 (current prices).

The growth of domestic demand will probably lose some momentum in 1971. Gross fixed asset formation in particular will increase less quickly, partly owing to the influence of government measures. For instance, capital expenditure by enterprises on industrial buildings, which increased very sharply in 1970, will be checked by the recently decided reintroduction of the building permit system for projects in the regions with the highest demand for skilled building workers. This system is to be superseded later by a temporary tax on investments in building and construction by enterprises in those regions.

Furthermore, a slower increase of investment in plant and machinery is also to be reckoned with, although the high degree of capacity utilization and the pressure to rationalize will remain major incentives to invest in 1971. The aggregate increase in investment by enterprises will therefore be less than in 1970, despite the extensive programme of aircraft purchases scheduled for the coming year. As regards public capital expenditure, central government investment in particular may well fall off, while a certain revival in investment by local authorities is to be reckoned with. Investment in residential construction, after declining in two successive years, is likely to show a fairly lively increase in 1971, more particularly thanks to state endeavours to give residential building projects more priority. On the basis of these various trends, the increase in gross fixed asset formation in 1971 can be put at about 11½% (current prices).

Stockbuilding will probably make a smaller contribution to production and employment than in 1970.

Private consumers' expenditure will certainly go on growing briskly in 1971. What is uncertain is the extent of this growth, which will be closely bound up with the development of the disposable income of households and their savings behaviour. Under the wage payment procedures laid down in most industries, wage earners will receive in 1971 part of the pay rises decided in the autumn of 1970. The wage bill may well expand almost as strongly as in 1970—in view, in particular, of the substantial pay rises laid down by the collective agreements covering a period of several years, and assuming that the tightness of the labour situation will laed to larger rises, if anything, when new agreements are made. But matters will be different if the Government introduces a temporary wage freeze. However, this was still not certain when the present Survey was drawn up. All in all, under the present circumstances and also in view of wage trends in the neighbouring countries, which provide important points of reference for Dutch workers and employers, the most plausible assumption seems to be that the increase in wages per employed person will be comparable to that of 1970. If we also allow for the restrictive effect which direct taxation will have in 1971 and assume a further perceptible increase in transfer income, then the disposable income of households should rise more slowly. It follows that private consumers' expenditure at current prices will not increase quite so much as in 1970, provided savings behaviour remains basically unaltered.

The growth of public current expenditure on goods and services will also depend on the use made of wage policy instruments. But even if the growth of wages in the public sector does not slow down markedly in 1971, the perceptible tendency for purchases of goods and services to settle at a more normal level will ensure that public current expenditure does not expand as rapidly as in 1970.

Although a somewhat slower growth of demand is to be expected in 1971, economic growth will continue to be governed mainly by the limited elasticity of supply, at least to begin with. The extensive investment programmes put through in recent years should admittedly make for a perceptible improvement in productivity. But the high degree of technical capacity utilization and the labour shortage will seriously impede the increase of production, especially if allowance is made for the further shortening of the working week, so that industrial production may well increase markedly less in 1971 than in 1970. A quicker growth of production in building and construction can only be achieved if productivity climbs more steeply, since the labour supply can hardly expand as much as in 1970. Assuming a normal increase in agricultural production and a slower expansion of the contribution of the services sector to the gross national product, the latter may expand by about 4% in 1971 (constant prices).

Strains on the labour market will continue to be fairly acute, especially since the expansion of the indigenous labour force is likely to lose momentum in 1971 after the appreciable increase of the two previous years. Since the level of unemployment in 1971 can hardly fall noticeably below the level recorded in autumn 1970, part of the additional labour demand will again have to be covered by recruiting foreign workers.

In view of the strains to which domestic supply will continue to be subject in 1971, and having regard to the considerable deliveries of aircraft, visible and invisible imports will again increase fairly sharply. But the slower underlying increase of demand and the probable changes in the structure of demand will prevent imports from rising so sharply as in 1970. Overall, however, there should be a further substantial deficit on current account despite the better trend in the terms of trade.

Although import prices will probably lose momentum markedly, domestic prices may well rise more sharply in 1971 than in 1970. Firstly, the pattern of supply and demand and the cost trend—the wage cost increase per unit of output will probably be the highest recorded in the Netherlands since 1966—will make for a further increase in prices. Secondly, consumer prices will also be under pressure from autonomous factors such as the increase in value-added tax rates from 12% to 14% on 1 January 1971 and the rent adjustment.

At a relatively early stage of the business upswing observed since 1967, the need to curb the increase in personal incomes and the expansive effects of government budgets had already been recognized by the authorities responsible for economic policy and the two sides of industry represented in the Economic and Social Council. In June 1969, the Economic and Social Council felt that the rise in wage costs per employed person should be limited in 1970 to about 7%, if prices rose by no more than 3½%. But the imbalances were aggravated relatively quickly by imported inflation and the excessive growth of domestic demand. The latter was due more especially to the sharp rise of households' disposable incomes—in particular of wages, which rose considerably more than the 7% mentioned—and the expansive effects of the budgets.

The stabilization programme announced in September 1970 underlines the determination of the Dutch authorities to get inflationary strains under control. The budget policy measures proposed for the 1971 budget year (details are given in the "Major economic policy measures" section are intended to help reduce the state deficit substantially, from the Fl. 2 200 million originally scheduled for 1970 to 1 500 million in 1971. The impact of these measures is even stronger in relation to the larger deficit given by the probable results for 1970 (2 900 million). Furthermore, the authorities intend to work for a "wage pause" whose details, however, have yet to be announced. In addition, a somewhat tighter money and credit policy, and retention or even intensification of price controls, will be applied.

This course of economic policy is undoubtedly in line with the requirements of the situation. But the prospects for the development of economic activity described above raise the question as to whether still greater efforts are desirable in the fields of public expenditure. For the budget policy measures are based primarily on higher taxation, which will be reflected at least partially in prices. In this connection it should also be said that the temporary increase of three percentage points in income tax rates for personal incomes and in corporation tax rates does no more than approximately counterbalance the loss of tax revenue caused by introduction of the second stage of the reduction in tax rates to offset the impact of price increases on taxable incomes in 1971. Despite the proposed cuts, public expenditure will probably, according to the forecasts, still increase three times as fast as the real gross national product. If a tighter rein cannot be kept on the increase in budget expenditure, efforts should at any rate be made to ensure that, when the budget is implemented, the expansion of public expenditure is substantially smaller in the first half of the year. Public orders should therefore be postponed as far as possible. A more restrictive budget policy would also, in particular, provide important guidelines for the behaviour of other parties in the economic process, more especially the two sides of industry. A recent opinion of the Economic and Social Council recommended supplementing the counter-cyclical application of the tax policy instruments by measures in the field of public expenditure. It may be added that on 12 November this Council has to pronounce on the whole stabilization programme which has been announced, and in December on the general pattern of economic policy in 1971.

A stricter budget policy would also ensure that the monetary and credit policy—whose scope is bound to be relatively limited in an open economy but which can nevertheless do much to check the expansion of capital expenditure—will not have to be relied on so heavily for management of the economy as in the past.

Major economic policy measures

July

(1) 5.3% increase in minimum weekly wages with effect from 1 July.

(2) Suspension of price provisions introduced in September 1969 and announcement of new measures for the compulsory notification of price increases for goods and services. Price rises based on an external cost increase are admissible and only have to be notified by firms with a turnover of more than Fl. 10 million; price rises based on other factors must be notified at least one months in advance. Such rises are, however, only authorized in order to ensure a return of not more than 7% on equity capital.

(3) 3% structural increase in pensions and grant of a 3% holiday allowance (6% in 1971) backdated to 1 January 1970.

(4) Amendment of the 1919 law on working conditions; ban on employment of young people aged less than 15.

August

(1) Intensification of the restrictive credit policy by establishment of new provisions, affecting commercial banks and agricultural credit institutions, concerning the sale of Dutch securities with redemption clauses.

(2) Publication of a law specifying that the minimum wage is to be raised on 1 July of every year by a percentage equal to the percentage increase laid down in the wage agreements of the previous year. The minimum wage for 1970 is thus raised to Fl. 157.50 per week, an increase of 2.5% on July.

(3) Tabling of a bill introducing, from 1 January 1972, an automatic correction of wage and income tax rates to allow for the incidence of inflation. The correction is based on the change in the consumer price index with allowance for alterations of indirect taxation and subsidies.

September

(1) Employers react to the flood of wage demands following the unofficial strike in the port of Rotterdam by recognizing the possibility of a special wage increase of Fl. 400 per employed person (about 3% of the annual wage bill) for the industries undergoing major stresses. The procedures for paying this differ from one branch to another. Many firms will not pay part of it until the first half of 1971.

(2) Prolongation of the restrictions on short-term bank loans to the private sector for the period from September to December 1970. Loans may not exceed average lendings in the last quarter of 1969 by more than 3.5%.

(3) Tabling of the draft budget for 1971. Although the increase in aggregate expenditure exceeds the forecasts for the 1971 budget year (13% after 11% in 1970), the state budget deficit is Fl. 2 100 million as against Fl. 2 200 million in the 1970 draft budget and a probable actual deficit of Fl. 2 900 million. Furthermore, announcement of a set of new measures to curb the increase in demand and to ease the strains on the markets for goods and services. In the budget policy sphere, independently of other measures to increase indirect taxation, there is to be a 3% counter-cyclical surcharge from 1 January 1971 on wages and income tax, corporation tax, motor vehicle tax and excise duties on petrol, plus introduction of a special tax for expenditure on building and construction by enterprises in the regions of the country with the worst labour shortages. Finally, the Central Government is to trim Fl. 140 million off its budgetary expenditure on investment. These measures may well reduce the 1971 budget deficit to Fl. 1 500 million. In the monetary and credit policy field, limitation on hire purchase of consumer goods, the personal loans granted by the banks for this and the

state guarantee for industrial building loans. In the incomes policy sphere, the authorities consider that the conditions are fulfilled for introducing the "wage pause" of Article 10 of the Wage Law. The Government has asked the Economic and Social Council to state its opinion on this point.

(4) Pending introduction of the aforementioned special tax, limitation of the number of non-residential building permits in the provinces with an acute labour shortage.

(5) Postal cheque offices brought within the scope of the measures to limit bank loans.

October

Tabling of a bill—in connection with increasing the flexibility of the tax policy arsenal for counter-cyclical reasons—empowering the Minister of Finance to change the most important tax rates by a maximum of 5%, for a period not exceeding one year.

November

Introduction of new price policy provisions for the period from 3 November 1970 to 16 March 1971, specifying the cost elements which may justify price increases; the Fl. 400 wage bonus conceded from September is one of these elements. In addition, abolition of the current arrangements for compulsory notification of price increases and the price freeze in force in various industries. Furthermore, the Government will not apply Article 8 of the Wage Law, which empowers it to introduce a general wage freeze.

Netherlands

TABLE 1 : **Key indicators**

	1965	1966	1967	1968	1969	1969
	% change by volume on preceding year					Indices 1963=100
Gross national product	5.4	2.6	5.8	6.7	5.1	140
Industrial production	6.3	5.9	5.7	10.6	8.2	158
Total imports	6.5	7.3	6.7	13.2	14.5	181
Private consumers' expenditure	7.4	3.4	5.2	5.9	4.0	136
Public current expenditure on goods and services	1.6	1.6	2.8	1.2	1.7	111
Gross fixed asset formation	4.9	8.5	8.1	11.6	0.6	163
Total exports	7.6	5.2	7.8	12.3	15.6	177
Gross national product per head of population	4.0	1.2	4.6	5.6	3.9	130
Gross national product per person in employment	4.5	1.8	6.1	5.8	3.6	132
	% change by value on preceding year					
Gross income per employee	11.7	11.1	9.2	8.7	11.2	191

TABLE 2 : **Indicators for internal and external equilibrium**

	1965	1966	1967	1968	1969
Balance exports less imports					
in million u.a.	+ 76	− 135	+ 23	+ 163	+ 91
as percentage of GNP	+ 0.4	− 0.6	+ 0.1	+ 0.6	+ 0.3
Unemployment rate	0.8	1.0	2.0	1.9	1.5
prices to private consumers (% change on preceding year)	+ 4.2	+ 5.4	+ 3.4	+ 2.6	+ 6.3

TABLE 3: Foreign trade (at current prices)

	% change on preceding year					Indices 1963=100	Million u.a.	% of totals
	1965	1966	1967	1968	1969	1969	1969	1969
Visible exports								
Total	+ 10.1	+ 5.6	+ 7.9	+ 14.5	+ 19.6	201	9 973	100
Intra-EEC	+ 10.2	+ 5.3	+ 6.7	+ 19.7	+ 25.1	226	5 993	60.1
To non-EEC countries	+ 10.0	+ 6.0	+ 9.4	+ 8.2	+ 12.1	172	3 980	39.9
Exports of food, beverages and tobacco								
Total	+ 13.0	+ 0.3	+ 9.9	+ 15.9	+ 15.4	182	2 311	23.2
Intra-EEC	+ 19.7	− 0.2	+ 9.6	+ 22.1	+ 19.6	215	1 549	15.5
To non-EEC countries	+ 3.6	+ 1.0	+ 10.5	+ 6.1	+ 7.8	139	762	7.6
Exports of raw materials, fuel and power								
Total	+ 7.4	− 0.4	+ 10.1	+ 12.8	+ 20.0	177	1 649	16.5
Intra-EEC	+ 3.4	− 0.7	+ 10.7	+ 22.5	+ 26.0	197	1 004	10.1
To non-EEC countries	+ 12.3	− 0.1	+ 9.5	+ 1.7	+ 11.7	152	645	6.5
Exports of semi-finished and finished industrial goods								
Total	+ 9.7	+ 9.7	+ 6.6	+ 14.4	+ 21.1	219	6 013	60.3
Intra-EEC	+ 8.1	+ 9.8	+ 4.5	+ 17.8	+ 27.5	243	3 440	34.5
To non-EEC countries	+ 11.7	+ 9.6	+ 9.0	+ 10.6	+ 13.4	191	2 573	25.8
Visible imports								
Total	+ 5.9	+ 7.5	+ 4.0	+ 11.5	+ 17.3	183	10 900	100
Intra-EEC	+ 8.7	+ 8.7	+ 5.0	+ 13.2	+ 19.2	199	6 132	56.3
From non-EEC countries	+ 2.9	+ 6.0	+ 2.9	+ 9.5	+ 15.0	165	4 678	43.7
Imports of food, beverages and tobacco								
Total	+ 3.5	+ 3.9	+ 11.3	+ 9.7	+ 19.0	181	1 487	13.6
Intra-EEC	+ 13.1	+ 8.8	+ 22.7	+ 28.1	+ 49.4	387	578	5.3
From non-EEC countries	− 1.2	+ 2.5	+ 7.6	+ 3.2	+ 5.4	135	909	8.3
Imports of raw materials, fuel and power								
Total	+ 1.0	+ 0.9	+ 5.2	+ 8.6	+ 13.8	157	2 214	20.3
Intra-EEC	+ 5.7	+ 7.7	+ 9 9.	+ 4.8	+ 3.0	115	445	4.1
From non-EEC countries	− 0.2	− 0.9	+ 3.9	+ 9.7	+ 16.9	160	1 769	16.2
Imports of semi-finished and finished industrial goods								
Total	+ 8.0	+ 10.5	+ 2.2	+ 12.8	+ 18.1	192	7 199	66.1
Intra-EEC	+ 8.0	+ 8.8	+ 3.3	+ 12.9	+ 18.1	195	5 109	46.9
From non-EEC countries	+ 8.1	+ 14.7	− 0.3	+ 12.6	+ 18.1	189	2 090	19.2

TABLE 4: Selected monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production	1968	*139.1*	*140.6*	*141.2*	*104.0*	*142.6*	*146.3*	*144.8*	*152.3*	*146.8*	*149.6*	*154.7*	*160.2*
(1963 = 100)	1969	*158.2*	*161.7*	*163.4*	*161.2*	*162.0*	*162.8*	*165.5*	*166.0*	*164.2*	*168.2*	*178.4*	*183.2*
	1970	*180.2*	*183.3*	*184.7*	*182.5*	*177.5*	*175.5*	*183.6*	*177.8*				
Unemployed	1968	*95.8*	*87.5*	*88.8*	*85.1*	*82.2*	*81.7*	*80.3*	*77.1*	*75.0*	*74.6*	*70.4*	*66.1*
(1 000)	1969	*69.4*	*68.7*	*69.9*	*64.7*	*64.1*	*63.2*	*63.9*	*65.1*	*63.3*	*62.5*	*61.3*	*62.9*
	1970	*61.7*	*57.6*	*56.7*	*54.4*	*55.0*	*54.4*	*51.7*	*52.2*	*53.8*	*55.9*		
Construction: permits for	1968	*13 356*	*8 029*	*11 468*	*12 158*	*12 670*	*11 398*	*8 303*	*11 519*	*12 074*	*8 873*	*7 987*	*12 690*
residential construction	1969	*9 893*	*8 959*	*12 663*	*11 359*	*10 793*	*9 869*	*6 864*	*14 414*	*11 130*	*9 431*	*10 454*	*13 010*
(1 000)	1970	*9 920*	*7 403*	*13 282*	*9 285*	*9 483*	*7 889*	*12 432*	*12 837*	*14 110*			
Private consumers' expen-	1968	*166*	*169*	*171*	*168*	*176*	*179*	*171*	*182*	*174*	*183*	*181*	*186*
diture: department store	1969	*170*	*191*	*196*	*192*	*210*	*198*	*186*	*206*	*197*	*202*	*200*	*222*
turnover (1963 = 100)	1970	*209*	*215*	*215*	*210*	*226*	*217*	*216*	*216*				
Consumer prices	1968	123.3	124.1	124.6	125.1	125.2	125.5	125.0	126.2	126.6	127.3	127.4	127.8
(1963 = 100)	1969	132.3	133.4	134.4	135.6	135.4	135.4	134.2	134.9	135.8	136.4	136.2	136.1
	1970	136.6	137.9	139.3	139.9	139.8	140.5	140.9	142.3	143.3	143.8		
Visible imports	1968	*823.0*	*721.7*	*747.9*	*704.9*	*815.1*	*672.8*	*775.2*	*798.3*	*775.9*	*836.0*	*816.8*	*811.2*
(million u.a.)	1969	*816.7*	*846.0*	*821.2*	*883.5*	*916.5*	*907.5*	*894.3*	*912.4*	*976.0*	*1 015.5*	*966.2*	*1 031.7*
	1970	*1 003.8*	*1 042.4*	*985.0*	*1 081.1*	*1 116.8*	*1 168.7*	*1 109.9*	*1 113.5*	*1 119.0*			
Visible exports	1968	*680.4*	*648.7*	*669.8*	*662.3*	*724.9*	*571.4*	*715.3*	*711.0*	*699.8*	*759.8*	*729.3*	*735.9*
(million u.a.)	1969	*745.2*	*766.9*	*797.5*	*780.3*	*815.9*	*823.7*	*839.9*	*864.3*	*873.8*	*916.6*	*851.7*	*875.0*
	1970	*900.3*	*959.0*	*946.3*	*994.2*	*928.6*	*949.6*	*992.9*	*1 017.2*	*1 003.4*			
Balance of trade	1968	*− 142.6*	*− 73.0*	*− 78.1*	*− 42.6*	*− 90.2*	*− 101.4*	*− 59.9*	*− 87.3*	*− 76.1*	*− 76.7*	*− 87.5*	*− 75.3*
(million u.a.)	1969	*− 71.5*	*− 79.1*	*− 23.7*	*− 103.2*	*− 100.6*	*− 83.8*	*− 54.4*	*− 48.1*	*− 102.2*	*− 98.9*	*− 114.5*	*− 156.7*
	1970	*− 103.5*	*− 83.4*	*− 38.7*	*− 86.9*	*− 188.2*	*− 219.2*	*− 117.0*	*− 96.3*	*− 115.6*			
Official gold and foreign	1968	2 194	2 164	2 082	2 028	2 008	1 988	2 000	2 030	2 001	1 972	1 968	1 967
exchange reserves	1969	1 892	1 937	1 954	1 981	2 046	1 965	2 031	1 999	2 005	2 502	2 235	2 090
(million u.a.)	1970	2 126	2 096	2 108	2 046	2 018	2 038	2 131	2 267	2 359			
Money supply	1968	*5 508*	*5 480*	*5 593*	*5 570*	*5 648*	*5 753*	*5 733*	*5 797*	*5 841*	*5 883*	*5 944*	*6 017*
(million u.a.)	1969	*6 066*	*6 065*	*6 076*	*6 071*	*6 175*	*6 191*	*6 163*	*6 197*	*6 231*	*6 467*	*6 415*	*6 486*
	1970	*6 512*	*6 493*	*6 650*	*6 698*	*6 840*	*6 805*	*6 919*	*6 931*				

Netherlands

NOTES TO GRAPHS AND TABLES

Source: Statistical Office of the European Communities (except as otherwise indicated).
Conversion into units of account (1 u.a. = 0.888671 g of fine gold = US $ 1) at the official exchange rates.

Graph 1

— Exports fob. Series adjusted for seasonal variations; three-month moving averages.

Graph 2

— Industrial production : excluding construction, food, beverages and tobacco; adjusted for seasonal variations; three-months moving averages.

Graph 3

— Labour market : series adjusted for seasonal variations; three-month moving averages; positie at end of month.

Graph 4

— Imports cif. Series adjusted for seasonal variations; three-month moving averages.

Graph 5

— Wages and consumer prices: indices of gross hourly earnings in industry (excluding mining, quarrying and construction); index of agreed wages. Cost-of-living index, source: CBS.

Graph 6

— Balance of trade : difference between seasonally adjusted imports and exports.

Graph 7

— Bank lending : short-term bank loans; end-of-period figures.

Table 1

— GNP at market prices.
— Industrial production: value added by industry.
— Total exports and imports: goods, services and factor income.
— Gross income per employee: income from paid employment, including employers' share of social insurance contributions.

Table 2

— Balance exports less imports: as defined for the national accounts.
— Unemployment rate; source: CBS; number of unemployed as percentage of the civilian labour force in employment.
— Prices to private consumers: price index of private consumption adjusted by the GNP deflator, computed from the national accounts.

Table 3

— Exports fob, imports cif; conversion at official exchange rates; the products have been regrouped on the basis of the Statistical and Tariff Classification for International Trade (CST): food, beverages and tobacco (Groups 0 and 1 CST), raw materials, fuel and power (Groups 2-4 CST), semi-finished and finished industrial goods (Groups 5-9 CST).

Table 4

— Industrial production: adjusted for seasonal variations, excluding construction and foodstuffs.
— Unemployed: end-of-month figures, adjusted for seasonal variations.
— Construction: seasonally adjusted number of dwellings authorized.
— Private consumers' expenditure: seasonally adjusted indices of department store turnovers.
— Consumer prices: not adjusted for seasonal variations.
— Imports cif, exports fob; conversion at official exchange rates; figures adjusted for seasonal variations.
— Balance of trade: difference between seasonally adjusted imports and exports.
— Official gold and foreign exchange reserves: gross reserves of gold and foreign exchange at end of month.
— Money supply: notes and coin in circulation excluding cash holdings of monetary institutions, plus sight deposits with credit institutions; seasonally adjusted end-of-month figures.

E. Belgo-Luxembourg Economic Union

Belgium

After a very sharp upswing of economic activity in 1969 the expansion of the Belgian economy levelled off somewhat in 1970. One of the factors responsible for this was the reduced elasticity of supply in numerous industries, but certain elements on the demand side also played a part. Export demand and investment in stocks, for example, made an appreciably smaller contribution to the growth of the economy than they did the year before. On the other hand, domestic final demand expanded very fast. The manpower shortage continued to be serious, though the situation on the labour market began to ease somewhat during the course of the year. In general the inflationary tendencies remained strong but, mainly because of the worldwide uptrend of prices, this was not reflected in a deterioration of current account; on the contrary, surpluses here grew considerably.

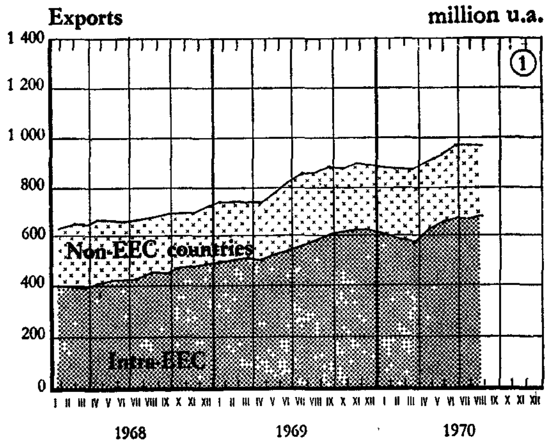
If anything, a further levelling-off of the expansion of demand is to be expected in 1971, on account of the less favourable prospects for sales of Belgian products to the leading trading partners. But the conditions for equilibrium may deteriorate, chiefly in view of the average rise in prices. Firstly, the upsurge of production costs has continued to be very sharp until recently; secondly, the introduction of value added tax may in itself spark off fresh tendencies for prices to rise if, owing to the deterioration in the costs situation of firms, they fail to take the desirable step of passing on the price reductions made possible by the change in the tax system. The result would be that the introduction of value added tax would not only bring about an alteration, implicit in the system, in the structure of prices, but also raise the average price level. Consequently, economic policy should be aimed primarily at getting both sides of industry to behave in a manner more consonant with the business situation; among other things, the present restrictive policy should not be relaxed too hastily.

1. Balance sheet for 1970

In 1970 the Belgian economy was still experiencing a marked boom. In the course of the year, however, growth slowed down because of a slackening in the expansion of demand, which had been very rapid, and also on account of the limited elasticity of domestic production. Persisting sharp strains on the markets for most goods and services, and a disequilibrium between available jobs and the number of persons seeking employment, brought about a vigorous upsurge of prices and costs, which, however, was less marked than in most of Belgium's trading partners. Consequently, the country's balance of payments position improved considerably by comparison with the year before.

This is all the more remarkable as *export demand,* which had played a decisive role in the upswing of economic activity in 1969, has been tending to slow down since the beginning of the year. The inflow of orders from abroad has declined in most industries, particularly in iron and steel and textiles.

According to customs returns the value of visible exports in the first eight months of the year was up by nearly 18% on the same period of 1969. For the whole year the growth rate may be put at some 16%, as opposed to 23.3% in 1969. Exports to the other EEC member countries, in particular Germany, again grew at an above-average rate, so that they now account for nearly 70% of all exports. On the other hand, the growth of exports to non-member countries was rather hesitant, owing, in particular, to the decline of demand from the United States.



As a whole, exports of goods and services as defined for national accounts may well have achieved a growth rate of 16% in terms of value, about a quarter of this being due to the rise in export prices

Unlike export demand, domestic final demand made a considerable contribution to economic activity throughout 1970. A decisive role was played by the exceptionally fast growth of *fixed asset formation.* Data so far available on deliveries of industrial capital goods from home and abroad seem to confirm the results of the EEC Investment Survey carried out in the spring, according to which the increase in expenditure on industrial investment could be over 50%. If this growth rate should, however, prove to be somewhat lower for the total year, it would be primarily because delivery bottlenecks have held up certain investment projects. The very strong propensity to invest is not only a consequence of the high degree of utilization of production capacity and the growth of firms' profits, but is probably also due to the fact that foreign firms have stepped up their investment programmes in Belgium very vigorously. In addition, the policy of improving the country's industrial structures was pursued actively, and this too was no doubt reflected in private investment.

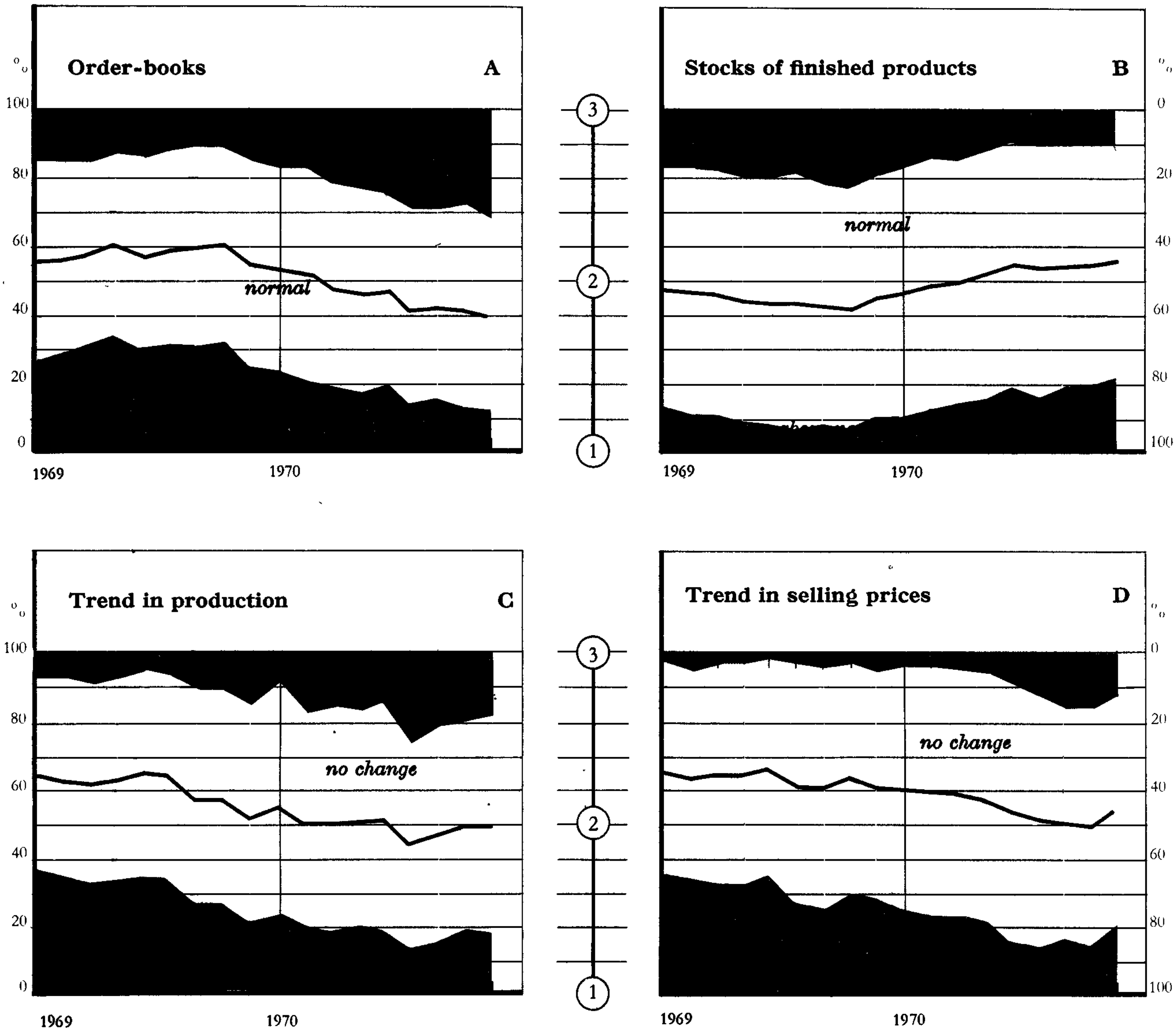
Public investment accelerated rapidly as a result of a fast expansion of road building by the Fonds des Routes, the associations of communes for building motorways and the communes themselves. The Central Government's expenditure in the stricter sense, on the other hand, seems to have changed little by comparison with 1969.

Despite certain difficulties in selling completed dwellings, and the effects of the restrictive credit policy, expenditure on residential construction probably continued to rise quite substantially, although towards the end of the year the pace unmistakably slackened. All in all, the value of gross fixed asset formation may have risen by approximately 15½% as against 11.4% in 1969.

By way of contrast, stockbuilding had an increasingly damping effect on total demand. Firms were very cautious about increasing stocks, partly because of the high cost of credit but also apparently in view of the coming into effect of value added tax. In addition, later in the year the tendency for the prices of raw materials and semi-finished products, in particular steel products, to fall on the world markets probably caused firms to run down their stocks.

A renewed, fast growth of total wages and salaries in the public sector helped the rather rapid expansion of public current expenditure on goods and services to continue. In addition, the growth of private consumers' expenditure over the year as a whole was also more marked: from 1969 to 1970 it could have been more than 9½% in terms of value. However, owing to the accelerated upsurge of prices, the real trend was practically the same as a year earlier. The growth of expenditure by households primarily reflects the more dynamic expansion of disposable incomes. The total wage and salary bill went up more than in 1969 (by about 12% as against 11%). Transfer incomes also increased considerably, and direct taxes on relatively low incomes were somewhat reduced. Furthermore, the savings ratio may have declined again in the second half of the year after a notable expansion in the first; this is in part the result of purchases made to beat the introduction of value added tax.

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



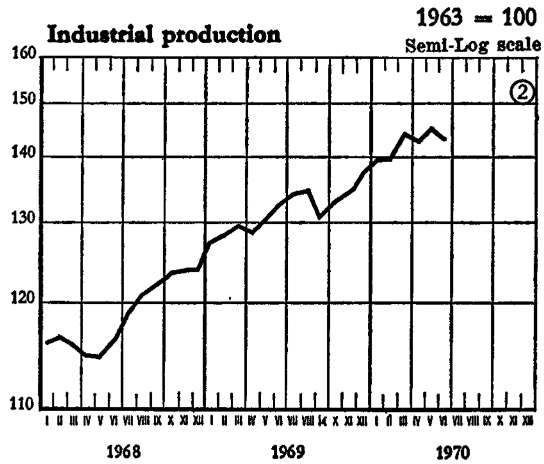
Answers to the questions in the EEC business survey, carried out in Belgium by the National Bank.

GRAPHS A, B, C and D : The three colours (green, yellow and red) show the percentages of the three different answers.

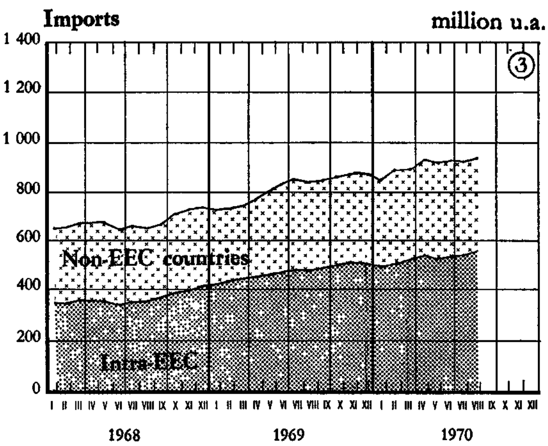
The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows :

by 0.03 for the answer "above normal", or "up";
by 0.02 for the answer "normal", or "no change";
by 0.01 for the answer "below normal", or "down".

The slackening of the expansion of domestic demand in the course of 1970 was due to quite a variety of reasons: capacity bottlenecks and difficulties in recruiting new staff, slower progress in improving productivity because of the high degree of utilization of the factors of production, but in certain industries, such as steel and some traditional consumer goods industries, also insufficient demand, which in its turn was the result of the stockbuilding situation mentioned earlier and, for example in textiles, the influence of fashion. For these different reasons the growth of industrial production has

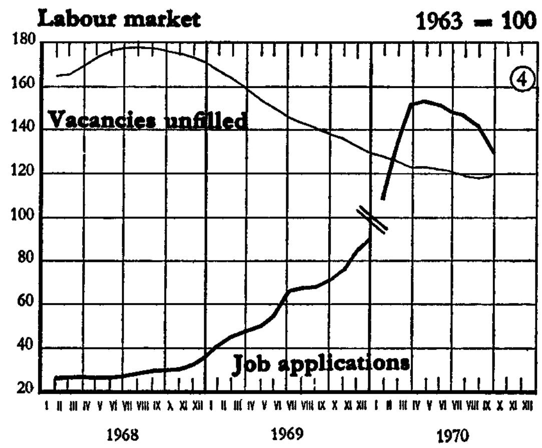


slowed down appreciably since the spring. In terms of value added at constant prices, the year-to-year growth was over 7% in 1970 as against 9% in 1969. In building and construction, on the other hand, production expanded more rapidly than in the previous year. In view of the likely trend of production in agriculture and services, gross national product at constant prices should have grown by about 5½% in 1970, as against 6.5% in 1969.



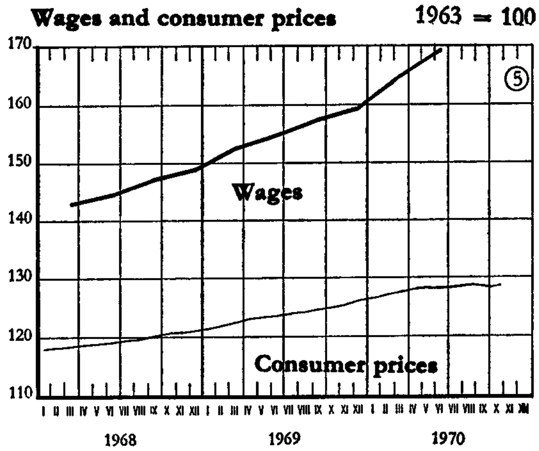
The growth of imports was far less lively than in 1969. Various factors played a role here. Purchases of raw materials and semi-finished products expanded appreciably more slowly than in the preceding year, and the growth of imports of finished goods was also below the 1969 level despite sharply increased purchases of capital goods. All in all the rise in imports of goods and services as defined for national accounts may be estimated to have been about 15% by value and 10½% by volume.

The labour market situation continued to be strained in 1970. The shortage of skilled workers was particularly serious. The number of persons in paid employment increased at a markedly slower pace (1.5% as against 2.5% in 1969). Additional requirements were covered chiefly by the natural growth of the labour force, a decrease in unemployment and some stepping up of immigration. Since the middle of the year, however, unemployment seems to have ceased to diminish. In September the unemployment rate [1] was 1.8%, as against 2.1% in the same month of 1969. The number of workers on short time has increased slightly of late.



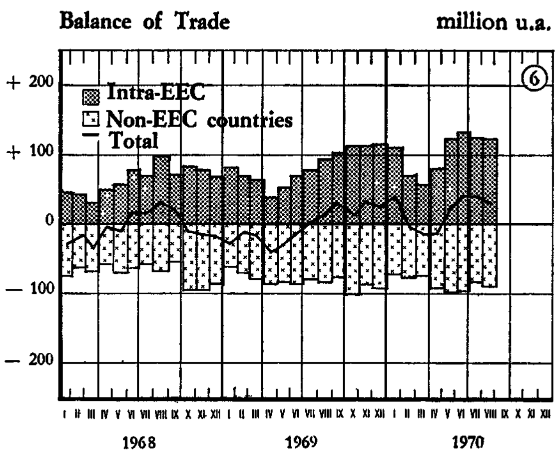
The price climate was still strained. Although the upward-driving tendencies have eased since the spring, the rise in prices on the various markets was, in annual average terms, greater than in 1969, an increasingly important factor pushing up prices being the rise in wage costs. In October the consumer price index was 3.5% higher than a year earlier.

[1] Seasonally adjusted figures for fully unemployed persons in receipt of benefit as percentage of the civilian labour force.



On the assumption of a non-seasonal acceleration in the fourth quarter, the rise in the consumer price index for the whole year may be put at some 4%.

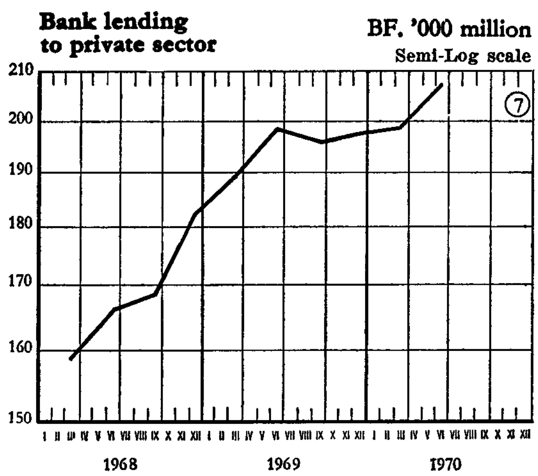
Since the fourth quarter of 1969 the current account of the Belgo-Luxembourg Economic Union has been showing large surpluses; the decisive reasons for this were the faster growth of exports than imports and a change in leads and lags in Belgium's favour. In the first nine months of the year the surplus on the basis of cash transactions totalled Bfrs. 27 300 million as against a deficit of Bfrs. 10 500 million in the same period of 1969. This exceptional situation is due mainly to the trend of the visible trade account, which registered a surplus of Bfrs. 17 800 million, whereas in the first nine



months of 1969 there had been a deficit of Bfrs. 14 400 million. Unlike current account, capital account showed an appreciable change: the surplus of Bfrs. 8 800 million registered from January to September 1969 was replaced by a deficit of Bfrs. 8 300 million in the corresponding months of 1970. This reversal of the trend is chiefly because the semi-governmental bodies did not contract any further loans abroad and because, despite the very considerable investments by foreign firms, the balance of direct investments diminished.

The overall balance of payments consequently showed a surplus of Bfrs. 16 700 million for the first nine months as against one of Bfrs. 100 million a year earlier. During the same period the Central Bank's net gold and foreign exchange reserves went up by Bfrs. 6 900 million, while the foreign currency position of the commercial banks and other financial institutions improved by Bfrs. 9 800 million.

As a result of the trade surplus domestic liquidity seems to have increased rather faster than in 1969. The expansion of the money supply (notes and coin and sight deposits) was, however, kept within limits, mainly owing to the restraint exercised by the bank of issue. In July the money supply was 6.6% up on a year before, for lending to firms and private individuals had a far less expansionary effect on the liquidity of the economy than in 1969; in the



first half of 1970 total lending was only 5.6% up on the December 1969 level, whereas the corresponding increase in the first half of 1969 had been 7.6%. Firms were able to cover their increased net financing requirements for fixed asset formation either through improved self-financing or a limitation of stocks. In September 1970 restrictions on bank loans to the private sector were appreciably relaxed.

Demand for and supply of goods and services

	1968 [1]	1969 [1]		1970 [2]		1971 [3]
	At current prices (in Bfrs '000 million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports [4]	422.0	+ 15.6	+ 21.1	+ 11½	+ 16	+ 9½
Gross fixed asset formation	218.2	+ 7.1	+ 11.4	+ 9	+ 15½	+ 5
Public current expenditure on goods and services	144.0	+ 7.5	+ 12.2	+ 5	+ 10½	+ 4
Private consumers' expenditure	660.7	+ 5.5	+ 7.7	+ 5½	+ 9½	+ 4
Gross national product	1 036.9	+ 6.5	+ 10.3	+ 5½	+ 10	+ 4
Imports [4]	418.8	+ 15.8	+ 19.8	+ 10½	+ 15	+ 9½

[1] Statistical Office of the European Communities.
[2] Commission estimates.
[3] Commission forecasts.
[4] Goods, services and factor income.

Note:
(*a*) The difference between the figures for demand and those for supply is accounted for by movements in stocks.
(*b*) The estimates and forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with experts from the member countries but are established and published on the sole responsibility of the Commission.

In 1970 the Government was able to reduce its net financing needs, which in 1969 still amounted to Bfrs. 28 000 million, i.e. over 2.5% of gross national product. This result seems due in the main to more moderate spending, for in the first nine months of 1970 budget cash expenditure went up by some 7.3% only, while a year earlier the increase had been 9.5%. The Government had less recourse to the money market but made considerable calls on the capital market, although a rate of interest of 8.5%—the highest ever—had to be offered on public loans issued in September.

In contrast to the capital market, the tendency on the money market, which reacts more sharply to inflows of liquidity from abroad, was marked by a slight easing in the course of the year, in line with developments on some important international markets. Consequently, the Central Bank reduced its discount rate on 22 October from 7.5 to 7%.

2. Outlook for 1971

Postponement of the introduction of value added tax by one year, which the Belgian Government decided in autumn 1969 by agreement with its partners in the Community, seems to have been opportune from the angle of short-term economic policy. For instance, in the course of 1970 the expansion of demand slackened appreciably. Nevertheless, those responsible for economic policy are still confronted by substantial problems, as the upsurge of costs and prices has continued to be very sharp in recent months.

Exports may well continue to be an important factor for expansion. Firstly, in 1970 the Belgian economy was able to improve its competitive position as regards costs. Secondly, owing to the high level of investment in the past year new, considerable capacities may be brought into operation which, in conjunction with some slackening in the expansion of domestic demand, will greatly increase opportunities for stepping up exports. Because of the probable slowdown of the expansion of demand in most other member countries, and the uncertainty regarding the extent of the increase in demand resulting from a recovery of the business trend in the United States and the United Kingdom, it is not certain that full advantage can already be taken of these opportunities. In view of the level already reached at the end of 1970 the growth rate of visible exports for 1971, in terms of value, is estimated at over 10½%.

It is expected that, as regards domestic demand, growth will switch from investment to consumer spending. For example, the propensity to invest may decline as a result chiefly of narrowing profit margins, persistent very high financing costs on the capital market, and less favourable sales prospects. This will influence actual capital expenditure particularly when current investment programmes are completed. In residential construction, too, expansion may fall off very appreciably as a result of the persisting rise in prices and the delayed effects of restrictive measures taken in this sector some time ago, especially since work on many residential buildings was speeded up to beat the introduction of value added tax. The trend of government capital expenditure may be strongly influenced by the expected distinct slowdown of spending by regional and local authorities. All in all, fixed asset formation should increase in terms of value by about 12% in 1971, over half of the increase being accounted for by higher prices.

Stockbuilding, on the other hand, may again make a bigger contribution to economic activity. Since firms ran down their stocks in 1970 prior to the introduction of value added tax, the situation in 1971 is likely to become rather more normal.

The fast growth of consumer spending in terms of money will probably continue. If there is no distinct change in households' propensity to save, private consumers' demand may even grow somewhat faster than in 1970. It is true that at the beginning of 1971 purchases made prior to the introduction of value added tax may temporarily cause a marked decline in private consumers' expenditure, but a tendency in the opposite direction may soon set in once again, owing to the increase in disposable incomes, for the rise in earnings per employed person will, as likely as not, accelerate further. The expiry of important wage agreements at the end of 1970 and the conclusion of a new "intertrade" wage agreement will play a decisive role here, especially as the negotiations will probably be conducted against the background of a still strained labour market. In general, adjustments of wages in accordance with the sliding wage scale—caused by rising prices and more frequent than in 1970—will also bring about a sharper growth of income from paid employment. Transfer incomes, too, will continue to grow fast, mainly because of the further raising of pensions and family allowances decided in 1970. A slight slowdown is to be expected only in income from entrepreneurial activity and property. All in all, private consumers' expenditure in money terms may be some 10% higher in 1971 than in 1970.

The utilization of technical production capacity, which had been exceptionally high in 1970, particularly in the first half, may decline if anything in some industries, especially iron and steel and other basic products, but considerable strains on the production system will still manifest themselves at the beginning of 1971. For industry as a whole, value added tax at constant prices may well increase by 4½% in 1971, so that the short-term growth of production would largely correspond to the long-term trend.

On the assumptions of a slower growth in building and construction and in the services sector and of a modest expansion of agricultural production, the real growth rate of gross national product will probably be a good 4% in 1971.

With such a growth of overall production, strains on the labour market may ease somewhat, especially in the second half of the year. In certain trades and areas, however, a great shortage of manpower may continue, particularly as the agreed working week is expected to be cut more sharply in 1971 than in 1970.

In view of the probable expansion of the various components of demand in 1971 it is likely that there will continue to be a quite lively, though slightly slower growth of imports. With a less rapid increase in exports and stable terms of trade the surplus on current account may, as a result, decrease appreciably.

Despite greater elasticity of domestic supply it is to be feared that the price level will rise faster than in 1970. The introduction of value added tax will in itself tend to push prices up through its mechanical effects not only on private consumers' expenditure, but also on public current expenditure on goods and services, and on public investments. Given the current demand/supply relationship and the accelerated rise in wage costs, it is questionable whether the opportunities for reducing prices in many branches as a result of value added tax will actually benefit the purchaser. The GNP deflator may consequently rise by over 5½%; this would be considerably more than was provided for with reference to the average price trend over the next five years in the guidelines in the draft Third Medium-term Economic Policy Programme.

The above forecasts show clearly that, while the inflationary boost given by demand pull will tend to slacken in 1971, the tendency for prices to rise as a result of cost push may become appreciably stronger. Under these circumstances, and partly because of the possible effects of the switch to the new tax system, short-term economic policy should continue to be aimed at controlling inflationary tendencies more effectively.

In the budget estimates submitted to Parliament for 1971, an increase by almost 10% is proposed for total expenditure, excluding the "contingency appropriations" to stimulate the economy. If expenditure financed outside the budget is included, the rate of increase amounts to some 12%. This is about three times as much as the growth of gross national product in real terms. The Government's net financing needs will remain relatively large, especially as there is considerable uncertainty about the tax receipts to come from value added tax in 1971. The strong boost which will be given to overall demand by some extra-budgetary or semi-government funds (association of communes for building roads, INAMI) also requires that budgetary expenditure should be managed very cautiously, especially at the beginning of the year. As much flexibility as possible is greatly to be desired, so that a switch can be made at the right moment to a more expansionary course should the growth of demand slacken further and the upsurge of costs and prices be replaced by a distinct trend towards stabilisation. In this connection it is to be welcomed that the budget estimates for 1971 provide some margin for investment expenditure through the 20% "contingency appropriations" in the extraordinary budget.

The cautious line of credit policy should be maintained for the time being, in particular as regards credit for consumption purposes. It would seem desirable, however, to change gradually from selective limitation of credit to general measures reducing liquidity, especially as the liquidity level of the economy is still quite high and certain types of firms may if anything be subject to less pressure on their liquidity as a result of the introduction of value added tax. Moreover, a cautious approach to credit policy would not conflict with a slight tendency for interest rates to come down, which is in harmony with the downturn of interest rates internationally.

In addition, if optimum conditions are to be achieved for changing over to the new tax system without major strains, closely concerted action between both sides of industry and the Government is needed. The aim should be to observe strict moderation at the beginning of the year in the matter of price formation and wage fixing. The authorities concerned already started working in this direction in 1970. The new tax measures were modified with the intention of diminishing the effects of value added tax on prices; furthermore, an active price policy was pursued in order to prevent unreasonable price increases. At the beginning of November new measures were decided on, to limit to the planned 2% the increase in the consumer price index caused by the "purely mechanical" effects of the value added tax. In particular, the interval between the reporting of price increases and their actual entry into effect was extended from one to three months, with the possibility for the authorities to extend it by a further two months. These measures will be successful only if both sides of industry, for their part, pursue a policy oriented towards stability. In this connection the wage and cost increases arising from the wage negotiations at the end of 1970 in some leading industries are of particular importance.

Major economic policy measures

June

In order to lessen the mechanical effects on prices of the introduction of value added tax as from 1 January 1971, the authorities transferred certains goods and services (services in the hotel and restaurant business, beverages, textile products and shoes) to a lower tax category. Consequently, the rise in the consumer price index caused by value added tax should be limited to about 2%. The reimbursement of value added tax on exports will be spread over two years. In addition, firms must make advance payments towards liability for value added tax.

July

(1) Various social measures were decided on: raising of pensions, of guaranteed incomes for elderly persons and of disablement benefit. Under the social programme for 1970/75, pensions and family allowances for self-employed persons are to be raised for the first time.

(2) Further extension (until 31 December 1970) of measures regarding the provisional granting of special aids for the speedy conversion and economic development of coalmining areas and some other areas which are faced with serious and pressing problems (law of 14 July 1966), and further special measures to deal with economic and social difficulties in some areas.

(3) Publication of the outline law of 15 July 1970 on the organization of economic planning and economic decentralization.

(4) Raising of the rates of turnover tax levied on imports of certain goods.

(5) Price policy measures (conclusion of a "programme agreement" to establish the profit margins for meat, a price freeze for soluble coffee, fixing of maximum prices for bricks).

(6) Publication of the Royal Decree fixing value-added tax rates and listing goods and services according to the rate applicable. The are four rates: 6, 14, 25 and 18%; the last is the normal rate.

September

Extension of credit ceiling measures until the end of 1970. A 17.4% increase is allowed for the whole of 1970, this being more than either the authorized (1.8%) or the actual expansion of credit (4.2%) in 1969. The new rate is only slightly less than the expansion of credit registered in 1968 (19.8%). The credit made available by this increase is to be used primarily to finance investment, large-scale exports and programmes benefiting the economic expansion of the country. The volume of consumer credit is frozen at the level reached at the end of September 1970.

October

(1) Tabling of a bill which, in connection with value added tax, introduces an export charge of 0.5% on products that at present attract a flat-rate export refund. The bill proposes a second rate at 1.75% for all other products, which represent 25% of exports. The tax burden of Bfrs. 4500 million amounts to half the tax burden to be removed by the introduction of value added tax.

(2) Submission of budget estimates for 1971. A balanced ordinary budget at Bfrs. 319 000 million is proposed, and an extraordinary budget at Bfrs. 55 000 million; this corresponds to a total increase in public expenditure of 9.9%. If certain supplementary expenditure is taken into account, the 9.9% increase may become about 12%. The extraordinary budget includes a contingency appropriation of 20% (against 27.5% in 1970).

(3) In accordance with the Central Bank's decision of May 1969, the rediscount quota was reduced to 9% of the banks' rediscountable assets. This quota, which was originally fixed

at 16%, had already been reduced to 10% at the end of March 1970 and to 9.5% at the end of June. At the end of September the available margin amounted to over Bfrs. 10 000 million, so that the regulations on the matter did not need to be relaxed.

(4) Lowering of discount rate by the Central Bank from 7.5 to 7% with effect from 22 October 1970.

November

Extension of the period for giving advance notice of intended price increases from one to three months, with the possibility for the authorities of extending this period by a further two months; methods of calculating net prices and profit margins are laid down, and existing penalties are made applicable under the new regulations.

Belgium

TABLE 1 : **Key indicators**

	1965	1966	1967	1968	1969	1969
	% change by volume on preceding year					Indices 1963 = 100
Gross national product	+ 3.8	+ 2.9	+ 3.8	+ 3.6	+ 6.5	131
Industrial production	+ 2.7	+ 4.9	+ 2.1	+ 4.1	+ 8.1	137
Total imports	+ 6.6	+ 8.1	+ 3.4	+ 13.2	+ 15.8	173
Private consumers' expenditure	+ 4.4	+ 3.3	+ 2.4	+ 5.7	+ 5.5	127
Public current expenditure on goods and services	+ 5.6	+ 4.1	+ 6.0	+ 4.0	+ 7.5	136
Gross fixed asset formation	+ 3.9	+ 6.4	+ 2.5	— 2.2	+ 7.1	134
Total exports	+ 7.7	+ 3.8	+ 6.7	+ 11.8	+ 15.6	171
Gross national product per head of population	+ 2.9	+ 2.2	+ 3.2	+ 3.1	+ 6.2	126
Gross national product per person in employment	+ 3.5	+ 2.5	+ 4.3	+ 3.6	+ 4.8	127
	% change by value on preceding year					
Gross income per employee	+ 9.5	+ 8.9	+ 7.1	+ 6.4	+ 8.4	162

TABLE 2 : **Indicators for internal and external equilibrium**

	1965	1966	1967	1968	1964
Balance exports less imports					
in million u.a.	+ 162	– 48	+ 176	+ 64	+ 186
as percentage of GNP	+ 1.0	– 0.3	+ 0.9	+ 0.3	+ 0.8
Unemployment rate	1.5	1.7	2.3	2.8	2.3
prices to private consumers (% change on preceding year)	+ 4.3	+ 4.3	+ 2.6	+ 2.1	+ 2.1

TABLE 3 : Foreign trade (at current prices)

	% change on preceding year					Indices 1963=100	Million u.a.	% of totals
	1965	1966	1967	1968	1969	1969	1969	1969
Visible exports								
Total	+ 14.2	+ 5.2	+ 3.0	+ 16.0	+ 22.9	207	10 038	100
Intra-EEC	+ 12.8	+ 6.1	+ 3.2	+ 18.5	+ 29.2	231	6 786	67.6
To non-EEC countries	+ 16.5	+ 3.9	+ 2.5	+ 11.7	+ 11.7	171	3 252	32.4
Exports of food, beverages and tobacco								
Total	+ 31.5	+ 8.4	+ 18.8	+ 15.5	+ 21.6	245	778	7.8
Intra-EEC	+ 31.6	+ 5.4	+ 25.7	+ 24.6	+ 26.8	290	665	6.6
To non-EEC countries	+ 31.3	+ 17.1	+ 1.3	− 13.4	− 1.8	130	114	1.1
Exports of raw materials, fuel and power								
Total	+ 3.1	+ 0.5	− 2.4	+ 13.4	+ 20.7	142	835	8.3
Intra-EEC	+ 1.4	+ 1.5	− 3.6	+ 10.8	+ 21.1	140	500	5.0
To non-EEC countries	+ 5.9	− 1.0	− 0.5	+ 17.4	+ 20.2	144	335	3.3
Exports of semi-finished and finished industrial goods								
Total	+ 14.4	+ 7.7	+ 2.3	+ 16.4	+ 23.5	215	8 425	83,9
Intra-EEC	+ 12.7	+ 9.8	+ 1.9	+ 18.7	+ 30.4	239	5 621	56.0
To non-EEC countries	+ 17.1	+ 4.2	+ 2.9	+ 12.8	+ 11.6	179	2 803	27.9
Visible imports								
Total	+ 7.6	+ 12.6	0	+ 16.1	+ 19.8	195	9 986	100
Intra-EEC	+ 10.1	+ 15.4	− 0.6	+ 14.8	+ 25.2	213	5 731	57.4
From non-EEC countries	+ 4.8	+ 9.1	+ 0.6	+ 17.8	+ 13.3	175	4 256	42.6
Imports of food, beverages and tobacco								
Total	+ 15.2	+ 8.1	+ 10.0	+ 2.8	+ 14.8	189	1 159	11.6
Intra-EEC	+ 22.5	+ 10.6	+ 11.8	+ 24.0	+ 23.3	269	642	6.4
From non-EEC countries	+ 10.6	+ 6.4	+ 8.6	− 13.1	+ 5.8	138	517	5.2
Imports of raw materials, fuel and power								
Total	+ 1.5	+ 1.1	− 2.1	+ 22.8	+ 11.2	157	2 193	22.0
Intra-EEC	+ 3.1	+ 5.2	− 5.5	+ 17.6	+ 15.3	157	782	7.8
From non-EEC countries	+ 0.6	− 1.3	− 0.2	+ 25.7	+ 9.0	157	1 410	14.1
Imports of semi-finished and finished industrial goods								
Total	+ 8.8	+ 18.3	− 1.1	+ 16.7	+ 24.0	215	6 634	66.6
Intra-EEC	+ 10.3	+ 18.4	− 1.1	+ 13.0	+ 27.5	221	4 307	43.2
From non-EEC countries	+ 6.2	+ 18.1	− 1.2	+ 23.6	+ 18.0	204	2 329	23.3

TABLE 4 : Selected monthly indicators

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production	1968	*114.8*	*115.1*	*117.3*	*111.0*	*114.6*	*124.0*	*116.9*	*123.6*	*125.9*	*119.5*	*125.0*	*126.4*
(1963 = 100)	1969	*130.5*	*127.8*	*130.9*	*126.7*	*133.2*	*136.9*	*130.7*	*135.2*	*125.8*	*137.0*	*140.4*	*134.3*
	1970	*143.5*	*141.0*	*149.7*	*137.8*	*149.0*	*143.5*	*144.0*					
Unemployed	1968	*99.2*	*99.9*	*103.4*	*104.2*	*104.4*	*104.3*	*104.4*	*103.6*	*103.4*	*103.6*	*101.4*	*99.6*
(1 000)	1969	*95.3*	*93.8*	*90.4*	*88.5*	*86.3*	*84.2*	*84.1*	*82.1*	*81.0*	*79.1*	*76.8*	*76.9*
	1970	*72.4*	*72.7*	*72.6*	*72.4*	*71.1*	*69.0*	*71.5*	*70.0*	*70.0*	*70.8*		
Construction : permits for	1968	*3 158*	*2 189*	*3 427*	*2 507*	*3 374*	*2 810*	*3 447*	*3 277*	*2 988*	*3 701*	*3 458*	*3 297*
residential construction	1969	*3 229*	*3 657*	*3 100*	*4 264*	*4 006*	*4 361*	*4 593*	*3 972*	*3 991*	*3 201*	*3 210*	*3 460*
(1 000)	1970	*3 126*	*2 898*	*2 283*	*3 721*	*2 677*	*2 792*						
Private consumers' expen-	1968	*128*	*133*	*133*	*133*	*139*	*135*	*136*	*141*	*134*	*134*	*145*	*138*
diture : department store	1969	*144*	*137*	*145*	*142*	*159*	*145*	*144*	*154*	*145*	*149*	*148*	*154*
turnover (1963 = 100)	1970	*158*	*155*	*158*	*156*	*165*	*162*	*164*					
Consumer prices	1968	118.20	118.27	118.38	118.63	118.76	119.18	119.41	119.52	120.00	120.46	120.48	120.91
(1963 = 100)	1969	121.44	121.96	122.62	122.95	123.32	123.65	124.10	124.28	124.64	125.14	125.70	126.20
	1970	126.73	127.12	127.85	128.33	128.35	128.40	129.07	129.34	129.30	129.52		
Visible imports	1968	*644.1*	*703.8*	*682.8*	*644.7*	*706.4*	*591.3*	*670.8*	*673.2*	*669.5*	*793.5*	*706.6*	*716.3*
(million u.a.)	1969	*765.9*	*746.3*	*763.7*	*813.8*	*830.6*	*853.2*	*891.3*	*805.0*	*867.4*	*915.9*	*827.6*	*862.7*
	1970	*841.0*	*940.6*	*877.7*	*1 021.8*	*860.8*	*942.4*	*1 013.4*	*886.7*				
Visible exports	1968	*617.8*	*671.7*	*645.6*	*701.6*	*663.3*	*627.5*	*728.3*	*682.3*	*672.5*	*749.9*	*701.8*	*720.2*
(million u.a.)	1969	*840.0*	*694.4*	*709.3*	*797.9*	*825.2*	*832.7*	*922.2*	*827.2*	*907.8*	*898.7*	*902.0*	*889.9*
	1970	*872.8*	*873.6*	*877.3*	*1 061.8*	*895.4*	*999.5*	*1 049.5*	*895.0*				
Balance of trade	1968	*− 26.3*	*− 32.1*	*− 37.2*	*+ 56.9*	*− 43.1*	*+ 36.2*	*+ 57.5*	*+ 9.1*	*+ 3.0*	*− 43.6*	*− 4.8*	*+ 3.9*
(million u.a.)	1969	*+ 74.1*	*− 51.9*	*− 54.4*	*− 15.9*	*− 5.4*	*− 20.5*	*+ 30.9*	*+ 22.2*	*+ 40.4*	*− 17.2*	*+ 74.4*	*+ 27.2*
	1970	*+ 31.8*	*− 67.0*	*− 0.4*	*+ 40.0*	*+ 34.6*	*+ 57.1*	*+ 36.1*	*+ 8.3*				
Official gold and foreign	1968	2 168	2 116	2 150	2 116	2 090	1 996	1 972	1 964	1 888	1 896	1 902	1 886
exchange reserves	1969	1 898	1 890	1 880	1 950	2 000	2 024	2 032	2 100	2 106	2 202	2 200	2 232
(million u.a.)	1970	2 240	2 232	2 250	2 270	2 178	2 196	2 280	2 302	2 360	2 406		
Money supply	1968	*6 953*	*6 965*	*7 081*	*7 114*	*7 174*	*7 206*	*7 159*	*7 238*	*7 238*	*7 261*	*7 335*	*7 349*
(million u.a.)	1969	*7 390*	*7 522*	*7 532*	*7 560*	*7 551*	*7 594*	*7 512*	*7 532*	*7 480*	*7 524*	*7 487*	*7 522*
	1970	*7 729*	*7 773*	*7 898*	*7 964*	*7 922*	*7 924*	*8 008*	*7 910*	*7 990*			

Belgium

NOTES TO GRAPHS AND TABLES

Source: Statistical Office of the European Communities (except as otherwise indicated).
Conversion into units of account (1 u.a. = 0.888671 g of fine gold = US $ 1) at the official exchange rates.

Graph 1

— Exports fob : series adjusted for seasonal variations; three-month moving averages.

Graph 2

— Industrial production : excluding construction, food, beverages and tobacco; adjusted for seasonal variations; three-month moving averages.

Graph 3

— Labour market : series adjusted for seasonal variations; three-month moving averages; position at end of month.

Graph 4

— Imports cif : series adjusted for seasonal variations; three-month moving averages.

Graph 5

— Wages and consumer prices: agreed wages for manual workers, all branches, source: Ministère du Travail et de l'Emploi; consumer prices, source: Ministère des Affaires Economiques.

Graph 6

— Balance of trade : difference between seasonally adjusted imports and exports.

Graph 7

— Bank lending : loans made by monetary institutions; end-of-period figures.

Table 1

— GNP at market prices.
— Industrial production : value added by industry.
— Total exports and imports : goods, services and factor income.
— Gross income per employee : income from plaid employment (including employer's share of social insurance contributions).

Table 2

— Balance exports less imports : as defined for the national accounts.
— Unemployment rate : number of unemployed as percentages of the civilian labour force in employment.
— Consumer prices: implicit price index of private consumption computed from the national accounts.

Table 3

— Exports fob, imports cif; conversion at official exchange rates; the products have been regrouped on the basis of the Statistical and Tariff Classification for International Trade (CST): food, beverages and tobacco (Groups 0 and 1 CST), raw materials, fuel and power (Groups 2-4 CST), semi-finished and finished industrial goods (Groups 5-9 CST).

Table 4

— Industrial production: adjusted for seasonal variations, excluding construction, food, beverages and tobacco.
— Unemployed: end-of-month figures, adjusted for seasonal variations.
— Construction: seasonally adjusted number of residential buildings authorized.
— Private consumers' expenditure: seasonally adjusted indices of department store turnovers.
— Consumer prices: not adjusted for seasonal variations.
— Imports cif, exports fob; conversion at official exchange rates; figures adjusted for seasonal variations.
— Balance of trade: difference between seasonally adjusted imports and exports.
— Official gold and foreign exchange reserves: gross reserves of gold and foreign exchange at end of month.
— Money supply: notes and coin in circulation, excluding cash holdings of the Treasury, the Central Bank and other banking institutions other than the Post Office giro; residents' sight deposits (up to one month) with banking institutions; sums held with the Post Office giro, the special Treasury accountants and non-residents; adjusted for seasonal variation; at end of month.

Luxembourg

In 1970 the Luxembourg economy was dominated by the appreciable falling-off in world demand for iron and steel products. However, the slowdown of overall economic growth was more moderate than in comparable phases of earlier business cycles, owing to the relatively more favourable trend in visible exports of the newly established industries and the continuing upswing of domestic demand. Real gross national product may have grown by 3½% in 1970 as against 7% in 1969. The slowdown of economic activity has, nevertheless, not yet had a beneficial effect on equilibrium. Overemployment persisted on the labour market, and the upsurge of prices and costs per unit of production accelerated appreciably.

The outlook for the economic trend in 1971 is dependent first and foremost on a very hesitant world demand for Luxembourg products and a slackening of domestic demand, in particular fixed asset formation. Despite a further slowdown of growth, the upward trend of prices and costs may continue vigorously.

1. Balance sheet for 1970

Expansion reached its peak in Luxembourg in the first quarter of 1970. Subsequently, economic growth slackened distinctly, owing to a deterioration in the international steel market, without, however, any notable easing of the severe cost and price strains. Over the year as a whole, production grew appreciably more slowly than in 1969.

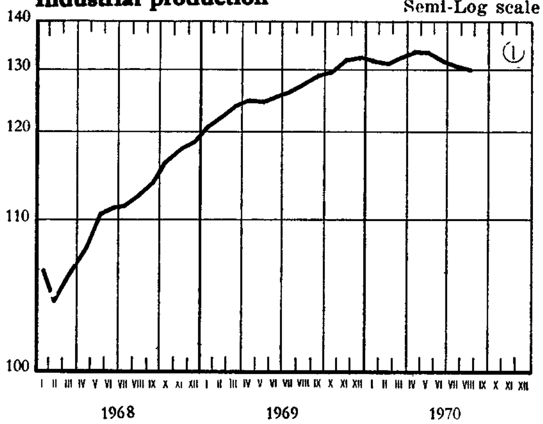
The distinct tendency for visible *exports* to slow down which established itself in the course of 1970 is due primarily to the perceptible slackening of demand for iron and steel exports, particularly in non-member countries. But it was also the result of the more sluggish trend of deliveries abroad by the newly established industries, especially chemicals. The increase in exports of goods and services in 1970 may be estimated in money terms at 8%, that is, about one third of the 1969 increase. Since the spring of 1970 the export prices of iron and steel products have been declining.

Unlike export demand, domestic demand tended to expand more rapidly than in 1969. Fixed asset formation has continued to grow vigorously, though capital spending by the Government and public corporations may as a whole have decreased. In the private sector, the most dynamic trend was again observed among the newly established industries and in iron and steel firms which carried out extensive programmes to increase capacity and rationalize production. Expenditure on residential construction also increased more rapidly, at least until mid-year. On account of the sharper upsurge of prices, which was very marked in building investment in particular, the increase in gross fixed asset formation was, at 27% in terms of value, even somewhat higher than in 1969.

Private consumers' expenditure, above all, was a decisive factor in the faster expansion of domestic demand. Government officials' salaries rose far more substantially than in 1969, and this led to a particularly stubborn upward trend of public current expenditure on goods and services. Households' consumption also gave the economy a far more vigorous boost than in the preceding year. Mainly on account of the accelerated rise in income from wages, this consumption must have risen, at current prices, by some 14½%, that is, nearly twice as fast as in 1969. Wages, particularly in the iron and steel industry and in building and construction, rose very fast following the entry into force of the new wage agreements at the beginning of the year and the appreciable raising of bonuses. The sliding wage scale contributed more than in 1969 to the increase in money wages. In addition, the total number of hours worked rose appreciably in 1970 as a whole, despite a distinct tendency to level off in the second half of the year. Transfer incomes also grew more sharply than in 1969; and the fact that the tax burden on households was lighter, owing to the adjustment of income taxe rates to make their progressive rise less steep, also played a part.

As the inflow of orders in the iron and steel industry declined, industrial production expanded distinctly more slowly from the first quarter of 1970 onwards. Over the whole year, industrial production—contribution to gross national

Industrial production 1963 = 100 Semi-Log scale

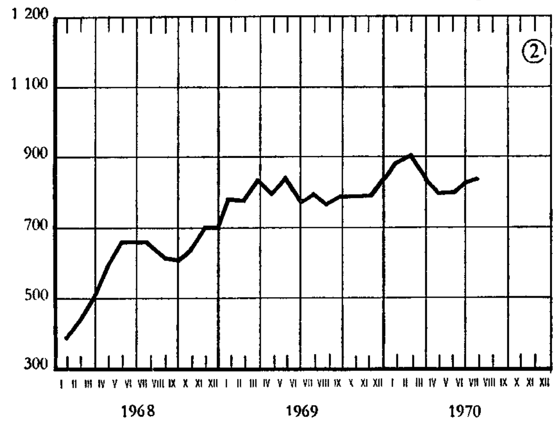


product at constant prices—will probably have expanded only by some 3%, as against 12.5% in 1969. By way of contrast, building and construction, despite a certain slowdown in the second half of the year, experienced a bigger expansion of production in one year than it had done for a long time past.

In view of the increased contribution of agriculture and services, the growth rate of real gross national product may be put at approximately 3½% in 1970 as against 7% in 1969.

The labour market continued to be characterized by pronounced overemployment, even though the first signs of an easing in the situation became apparent as the year went on, especially because the number of persons employed in the traditional industries ceased to grow. The net additional manpower requirements, which were particularly high in the new industries and building and construction, amounted to an esti-

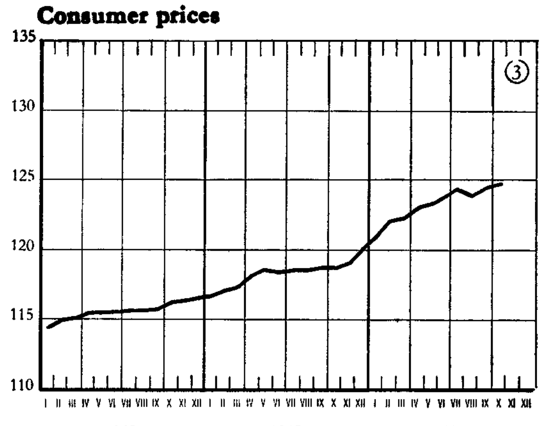
Vacancies unfilled number



mated 2% or so for the year as a whole. Once again they were covered by the recruitment of foreign workers, who in 1970 accounted for one fifth of total employment—a record level.

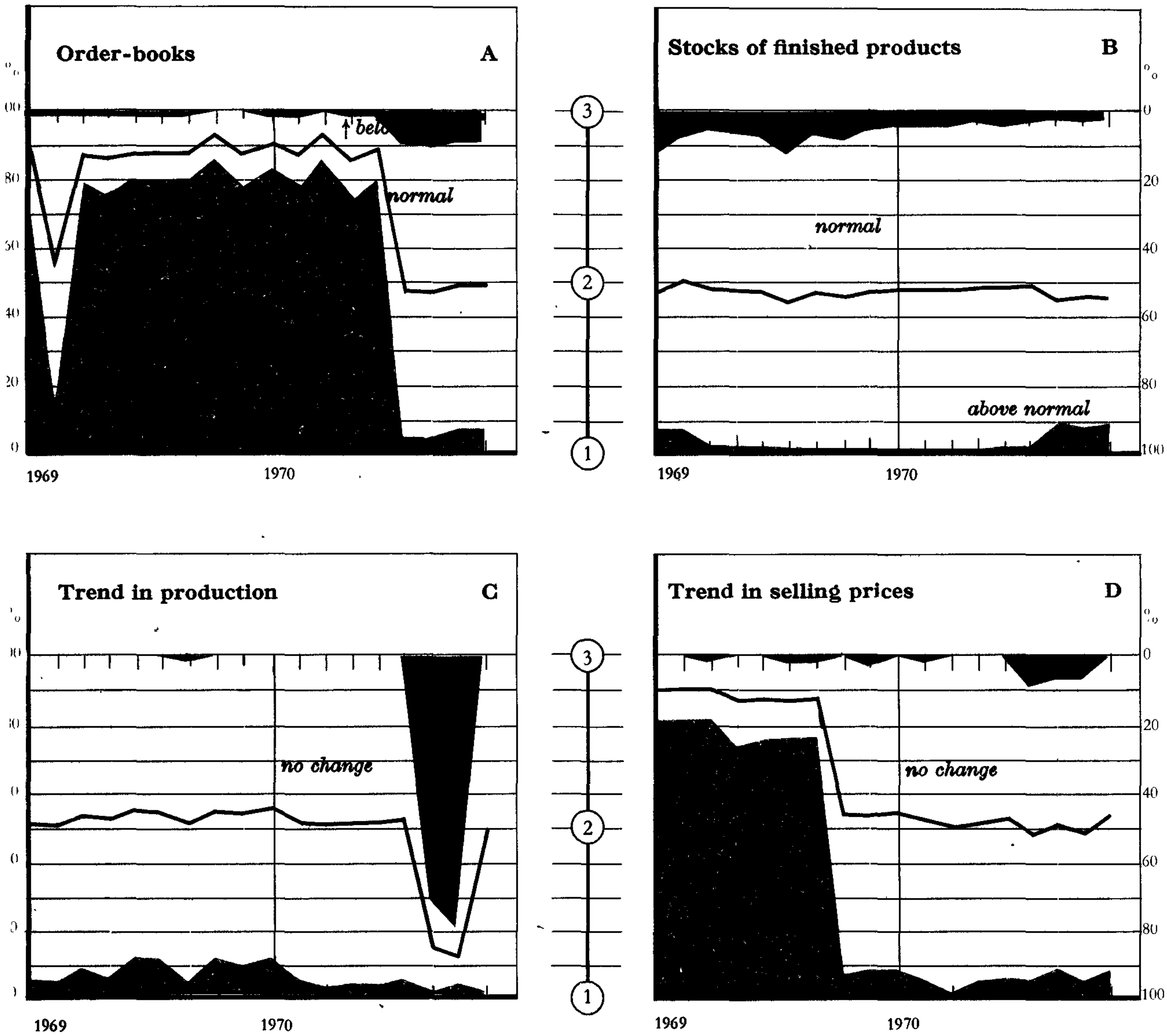
The import trend was chiefly influenced by the accelerated growth of demand for consumer and capital goods, and less by the slower expansion of exports and production. Consequently, imports continued to grow very strongly (by some 17% at current prices) and this brought about an appreciable deterioration in the balance of exports less imports, to which the less favourable trend of the terms of trade also contributed.

Consumer prices



The price trend was marked at the beginning of the year by the changeover to value added tax. Measures taken by the Government enabled the consequent price rises to be kept within bounds. Between November 1969 and January 1970 the

BUSINESSMEN'S VIEWS ON THE INDUSTRIAL SITUATION



Answers to the questions in the EEC business survey, carried out in Grand Duchy of Luxembourg by STATEC.

GRAPHS A, B, C and D : The three colours (green, yellow and red) show the percentages of the three different answers.

The black curves, the scale for which is given between the graphs, show the figures obtained by adding together the percentages weighted as follows :

by 0.03 for the answer "above normal", or "up";
by 0.02 for the answer "normal", or "no change";
by 0.01 for the answer "below normal", or "down".

Demand for and supply of goods and services

	1968 [1]	1969 [1]		1970 [2]		1971 [3]
	At current prices (in Lfrs '000 million)	% change on preceding year				
		Volume	Value	Volume	Value	Volume
Exports [4]	30 808	+ 13.0	+ 22.0	+ 4	+ 8	+ 2
Gross fixed asset formation	9 528	+ 16.0	+ 24.7	+ 16	+ 27	— 5
Public current expenditure on goods and services	4 546	+ 2.1	+ 5.7	+ 2	+ 13	+ 3
Private consumers' expenditure	23 163	+ 5.0	+ 7.4	+ 8½	+ 14½	+ 4½
Gross national product	37 926	+ 7.0	+ 15.0	+ 3½	+ 10½	+ 2½
Imports [4]	29 919	+ 14.5	+ 18.8	+ 12	+ 17	+ 1

[1] Service central de la statistique et des études économiques (STATEC), Luxembourg.
[2] Commission estimates.
[3] Commission forecasts.
[3] Goods, services and factor income.

Note :
(*a*) The difference between the figures for demand and those for supply is accounted for by movements in stocks.
(*b*) The estimates and forecasts are approximations based on certain hypotheses, generally mentioned in the Quarterly Surveys. They have been discussed with experts from the member countries but are established and published on the sole responsibility of the Commission.

consumer price index went up by about 2%. In the further course of the year, however, the strong non-seasonal tendency for prices to rise persisted. An important contributory factor was the appreciable increase in the cost of imports and the relatively sharp rise in the prices of services. As a result the consumer price index was 5.1% higher in October than a year earlier.

2. Outlook for 1971

The trend of demand, production and employment in 1971 should be less expansive than in 1970.

The prospects for world demand do not suggest that there will be a considerable growth of exports from Luxembourg in the short term. At best, only a very modest increase in exports of iron and steel products is expected, on account of the situation in the leading customer countries. The same applies, though less so, to exports of other industrial products from Luxembourg. It is therefore probable that, despite the bringing into operation of fresh production capacity, exports of goods and services will make hardly any progress in terms of value, compared on a year-to-year basis.

Domestic demand is likely to grow more slowly, mainly owing to the expected stabilization of expenditure on fixed asset formation. Although a renewed increase in capital expenditure is to be anticipated in mechanical engineering and chemicals, the propensity to invest in the iron and steel industry will probably fall off quite sharply. In addition, is is doubtful whether demand for residential construction will continue to grow perceptibly, in view of the sharp rise in costs. Government investment expenditure, on the other hand, should expand quite vigorously in 1971.

Consequently, the economic trend in 1971 should be marked even more than in 1970 by a consumer boom. On the one hand, public current expenditure on goods and services should make an appreciable contribution, especially as civil servants' salaries were raised by 6.5% at the end of 1970. On the other hand, households' income and consumption will continue to rise substantially; the operation of the sliding wage scale will play a major role here. In important industries, however, such as iron and steel, wage and salary increases may be smaller than in 1970; and the total number of hours worked in 1971 may register no further increase. If it is assumed that propensity to save will remain static, and if purchases made in the autumn of 1970 before the entry into force of higher rates of value added tax are taken into account, private consumers' expenditure should increase in 1971 by about 9% in terms of value.

With so much less activity in the iron and steel industry, industrial production will probably increase by hardly more than 2% in 1971. Building and construction will likewise hardly exceed the 1970 level. All in all, therefore, it is currently expected that the growth of gross national product from 1970 to 1971 will be less than 2½%.

On the labour market, the tendency towards an easing of the situation is likely to assert itself more distinctly, at least in so far as the need for further manpower, which will be appreciably less than in 1970, can be covered more easily by recruiting foreign labour. Demand in the traditional industries and in building will diminish rather than otherwise, while additional manpower will probably again be sought by the new industries and by the services sector.

As a result of the renewed slackening of demand and production, an appreciably more sluggish trend of imports is also to be expected. The balance of exports less imports, at any rate, may continue to show a heavy deficit in 1971, in particular because of a further deterioration of the terms of trade.

The demand/supply situation could provide the conditions for a distinctly calmer price climate. However, there are factors militating against this, such as the persisting upsurge of wage costs, which has even accelerated recently, the higher prices of imports, especially those coming from Belgium, which provides Luxembourg with about one third of its imports, and the increase of indirect taxes. It is therefore to be feared that the rise in consumer prices will fall not far short of the already relatively steep rise in prices in 1970.

Until now, short-term economic policy in Luxembourg has largely been determined by the need to dominate inflationary tendencies. During the whole of 1970 the Government endeavoured to create a better balance between supply and demand, and to damp down the upsurge of costs, in particular with the help of measures provided for in the stabilization programme of November 1969. The most important guidelines in this programme have already been discussed in earlier Quarterly Surveys.

Despite the less favourable prospects for growth in 1971, economic policy will have to follow the same course in the coming months as in 1970, because of persistent internal disequilibria. In this connection it should be noted, with reference to budget policy, that the budget estimates for 1971 provide for a considerable reduction in the deficit to be financed—it should drop from Lfrs. 1300 million in 1970 to Lfrs. 900 million. This result is all the more remarkable as it is to be accompanied by a very sharp increase in public expenditure—11.4% more than in the budget estimates for 1970. In order to ensure non-inflationary financing of the additional expenditure, the Government has laid before Parliament measures to increase direct and indirect taxes (exceptional "contingency" surcharge on firms' profits, raising of value-added tax rates and introduction of a temporary consumer tax on some kinds of liquid fuels). The additional revenue expected as a result of these measures amounts to Lfrs. 450 million (that is, about 3½% of total expenditure).

In the longer term these measures also help to balance the budget. In the short term, however, they pose problems, as the surcharge on firms' profits will not be removed until an easing of the demand/supply situation is already in the offing and investment by enterprises in particular is liable to decline. The raising of indirect taxes is bound to affect the level of consumer prices, though it will be a move towards the harmonization, desirable in the longer term, of value-added tax rates within the Community and of the structure of tax revenue from the angle of the breakdown into direct and indirect taxes. In order to prevent excessive price increases as a result of the raising of value-added tax rates, the price policy pursued hitherto should be maintained for some months and perhaps even be intensified.

Special efforts also seem necessary to bring the management of expenditure by the public authorities into line with short-term economic requirements. The proposed increase in expenditure is appreciably larger than the average increase provided for in the medium-term financial plan. It is to be feared, moreover, that this proposed increase, which is already very substantial, will be even larger if higher prices lay a heavier burden on the public authorities. From this angle, too, it is in the interest of the public authorities to back the campaign against inflation with a policy on expenditure, in particular by keeping the rate of expansion of public expenditure in the first half of the year well below that of the rise in expenditure planned for the whole year.

Major economic policy measures

July

(1) Publication of the law of 17 June 1970 on restrictive trade practices. Agreements involving a limitation of free competition and abuse of dominant positions by firms are now punishable.

(2) Prolongation of the provisional tax concessions for investment purposes granted under the law of 5 August 1967.

(3) Prolongation until the end of the year of the reduced value-added tax rate for certain foodstuffs and pharmaceuticals, tobacco products and hotel and restaurant charges.

August

Submission of the budget estimates for 1971. The increase in total expenditure is estimated at 11.4% (12.9% for ordinary expenditure and 5.4% for extraordinary expenditure); these rates of increase are, however, considerably lower than those of actual expenditure in 1970. Thanks to a relatively fast growth of tax revenue (14.6%) the deficit will go down from 1270 million in 1970 to 885 million in 1971. Additional revenue totalling Lfrs. 450 million is expected from an increase in the tax burden: introduction of an exceptional contingency surcharge, limited to 1971, on companies' profits and a special consumer tax on certain types of liquid fuels; in addition, the value-added tax rates are raised from 8 to 10% (normal rate) and from 4 to 5% (reduced rate). It is also proposed that the reduced value-added tax rate (2%) introduced at the beginning of 1970 should be extended until the end of 1971.

October

(1) Fixing of maximum profit margins for central heating installations, maximum prices for beverages, and selling prices for household coal.

(2) Further raising of the guaranteed minimum wage to Lfrs. 36 an hour and Lfrs. 7200 a month.

Luxembourg

TABLE 1 : **Selected monthly indicators**

	Year	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Industrial production (1963 = 100)	1968	*101.8*	*104.1*	*110.6*	*108.6*	*111.3*	*112.2*	*109.7*	*114.6*	*117.1*	*116.2*	*118.5*	*119.6*
	1969	*122.1*	*123.4*	*125.5*	*124.6*	*122.6*	*127.8*	*126.1*	*127.4*	*130.7*	*129.8*	*133.6*	*131.8*
	1970	*127.1*	*132.4*	*136.0*	*132.0*	*132.0*	*130.5*	*129.0*	*129.4*				
Unfilled vacancies	1968	*456*	*499*	*517*	*728*	*737*	*651*	*586*	*577*	*645*	*692*	*751*	*670*
	1969	*890*	*744*	*829*	*823*	*855*	*656*	*879*	*743*	*744*	*756*	*833*	*922*
	1970	*904*	*875*	*710*	*820*	*876*	*774*	*872*					
Construction : permits for residential construction	1968	*29*	*12*	*17*	*16*	*18*	*9*	*23*	*15*	*19*	*14*	*22*	*14*
	1969	*16*	*23*	*11*	*29*	*11*	*58*	*26*	*27*	*15*	*35*	*27*	*20*
	1970												
Consumer prices (1963 = 100)	1968	114.24	114.83	114.95	115.19	115.09	115.19	115.41	115.40	115.59	116.12	116.29	116.74
	1969	116.96	117.08	117.30	117.57	118.08	117.94	118.26	118.11	118.31	118.39	118.77	120.03
	1970	121.21	121.98	122.21	122.74	123.38	123.72	124.20	123.84	124.34	124.73		

NOTES TO GRAPHS AND TABLES

Source: Statistical Office of the European Communities (except as otherwise indicated).

Graph 1

— Industrial production: excluding construction, food, beverages and tobaeco; adjusted for seasonal variations; three-month moving averages.

Graph 2

— Unfilled vacancies: series adjusted for seasonal variation; three-month moving averages.

Graph 3

— Consumer prices; source: STATEC.

Table

— Industrial production: adjusted for seasonal variations, excluding construction and foodstuffs.
— Unfilled vacancies: seasonally adjusted end-of-month figures.
— Construction: seasonally adjusted number of residential buildings authorized.
— Consumer prices: not adjusted for seasonal variations.

Brussels, 7 July 1970

Commission memorandum to the Council on the economic situation in the Community

For two years now, boom conditions have prevailed throughout the Community.

Although the rise in exports to non-member countries has slackened somewhat, the growth of internal demand continues to be reflected in a rapid pace of economic activity and a strong upward thrust of prices, reinforced by the inflationary process that has developed in the world. Since the autumn of 1969, the trade balance of certain member countries has tended to deteriorate.

While in most member countries economic activity appears to be reaching an upper limit, the current prospect in the Community is for incomes to rise and investment to expand, making it unlikely for demand in the second half of 1970 to develop in a way that will bring about a reversal in the economic trend during that period. In addition, cost inflation is liable to pose difficult problems to those responsible for economic policy, particularly if in certain Community countries it goes hand in hand with a less rapid pace of expansion.

The measures which the Member States had decided to take jointly, following the Council sessions of July 1969 and January 1970, with a view to achieving more balanced growth, have not yet produced the expected results, except for minor improvements. Urgent political or social problems have often limited the governments' room for manœuvre. In some cases, major social conflicts have complicated their task and sometimes added to the disequilibria. Inflation also helps to mitigate or mask certain difficulties, even though these effects are shortlived and illusory.

The uncertainties surrounding the international business situation, like the persistence of disequilibria within the Community, make it necessary for the Member States to exercise great caution in short-term economic policy so as to ensure that the inevitable adjustments will not be painful and long. A return to a sound business trend is all the more desirable as it would provide a firm economic basis for the economic and social reforms which large sections of public opinion in the Community countries expect and which should be part of a medium-term policy of balanced growth.

I. Economic developments and outlook

1. *International background*

In the first half of 1970, the world economic trend came increasingly under the influence of the slowdown in economic activity in the *United States.*

The real gross national product of the United States, which had run level in the last quarter of 1969, declined by 0.8% in the first quarter of 1970 and, to judge by the (incomplete) information available for the following quarter, there is little likelihood of an upturn having set in since. In May, the index of industrial production fell further; it was 3.2% lower than in July 1969, i.e. before the trend was reversed. In May, 5% of the civilian labour force were unemployed, while a year earlier the rate was about 3.5%.

Despite the efforts which the American authorities made to eliminate inflationary pressures, consumer prices continued to soar (at an annual rate of 6% during the first five months of the year). Only for finished goods has the price trend tended to moderate since the beginning of the year. During the same period, visible imports ran level while exports continued to go up. The trade balance increasingly improved; in the first five months of 1970, there was a surplus of $1130 million, as against $135 million during the same period in 1969.

Given this situation, the chances for a significant recovery in the months ahead are difficult to assess. Some factors undoubtedly help to stimulate demand. Budget transactions have currently closed with a deficit that is mainly attributable to tax alleviations, a slower rise in tax receipts as a result of the slackening of economic activity, a salary increase for officials, and higher welfare payments. In April, the resulting increase in disposable incomes led to a rise in consumption of households; at the beginning of the second half of the year, this consumption may have received additional stimuli from the fresh reduction in income tax, which came into force on 1 July 1970. Moreover, the line of monetary policy has been less restrictive for some time past. The fall in corporate profits, on the other hand, is affecting investment plans, as can be seen from the latest investment survey by the Department of Commerce. The stockbuilding cycle has entered a phase of contraction.

Although there is very little likelihood of the recession gathering momentum, any revival in economic activity that occurred before the end of the year would hardly be very vigorous.

In the *United Kingdom,* the improvement in the overall balance of payments in 1969 and the first quarter of 1970 permitted repayment of substantial parts of the country's foreign debts, which were reduced by a total of $4100 million during that period. This achievement, however, was possible only through a very modest advance in industrial production, whose index in March-April was only 2.5% up on a year earlier, and through an increase in unemployment, while consumer prices went up vigorously (4% in the first five months of 1970).

For the months ahead it is expected that private consumption, influenced by substantial wage awards, will rise significantly, which is bound to strengthen the expansion of production and the propensity to import. In the circumstances, the deterioration in the trade balance suggested by the figures for April and May could persist during the second half of 1970.

Various *other European countries,* particularly Denmark, Norway, Sweden and Spain, where there are major internal and external imbalances, will be prompted to dampen demand, and this will check the rise in imports.

Similarly, those *raw material producing countries* which have particularly close trading relations with the United States, or whose foreign exchange reserves have fallen recently, may curb their purchases abroad.

Under these various influences, the current slowdown in the growth of world trade is liable to become more pronounced in the second half of 1970. Estimates made by the Commission's staff show that in 1970 the rise in world trade, excluding intra-Community trade and trade with the countries of the Eastern bloc, will, in terms of value, probably be no more than 8.5%, as against 11% in the previous year.

The trend in international payments, which had largely calmed down after the changes in the parities of the French franc and the German mark, has of late been affected by disturbing influences which in the long run may lead to new unrest.

The overall balance of payments of the United States is still closing with a heavy deficit; in the first quarter of 1970, it was $1700 million, on a liquidity basis. This deficit, whose effects are amplified by the Euro-currency market, which has a dynamism of its own, thus leads to the creation of new international liquidities at a pace that, in the current climate of general inflation, could be considered excessive. Despite this trend, the tendency, observed until the beginning of April, for short-term interest rates to decline, has been reversed since; this bears witness to the extremely lively expansion of international demand for means of finance and to the persistence of a rapid pace of inflation in the main industrialized countries. The unstable nature of such a situation must be emphasized. There is in fact reason to fear that new disruptions will occur in the balance of payments trends if the trend in prices or economic activity changes substantially in one or more large countries. Unless the inflationary strains are eliminated rapidly, adjustment to a changed international business trend could become difficult for countries faced with particularly vigorous rises in prices and costs.

All in all, the international background to the economic trend in the Community shows itself to be uncertain for the next few months.

2. *The economic situation in the Community*

Inflationary strains in the Community have remained strong during the past few months. Even where the pressure of domestic demand has started to ease, as in France, prices have climbed further, forced up by the rise in costs, which increasingly takes on an autonomous character.

In most member countries, the expansion of consumption and investment was very lively in the first half of the year, offsetting the weaker trend in demand from non-member countries. Despite appreciable advances in output—in the first four months of the year, industrial production in the Community as a whole rose at an annual rate of some 10%—and despite heavier reliance on imports, the gap between supply and demand remained substantial. The degree of capacity utilization is still very high. In all countries, shortages of manpower considerably hamper efforts to step up production in line with increasing sales possibilities. This is the case even in France and Italy, where regional disparities or a lack of suitably skilled workers among those available make it more difficult for industry to recruit additional manpower than is suggested by overall unemployment statistics.

In most member countries, orders on hand have gone up further and delivery times have lengthened. The rise in costs, particularly wage costs per unit of output, which had already been considerable last autumn, has gathered additional momentum. The moderating influence which this rise could indirectly exert on investment by narrowing the scope for self-financing has been weak so far because, in the current inflationary situation, firms have not found it difficult to put up their selling prices. It is therefore hardly surprising that the investment plans of industrial firms for 1970, which at the end of 1969 had already been up by 15 to 57% varying with the country, were revised further upwards, as was revealed by a survey carried out in April-May 1970 on the initiative of the Commission's departments.

As regards wage and salary incomes, the collective agreements concluded in the recent past have brought very substantial increases that greatly exceed productivity gains; in the first quarter of 1970, hourly wage rates in practically all member countries were 10 to 16% up on a year earlier, and the increase in wages actually paid was generally higher still. There is little doubt that the upward thrust of wages and salaries will remain strong in the next few months. In addition, in the countries which apply sliding wage scales, the faster rise in consumer prices will lead to corresponding adjustments in wage rates. There are therefore self-reinforcing elements in the inflation which are liable to remain effective for some time yet.

It is no doubt due to the worldwide character of the inflation that the deterioration in the current account of most Community countries has so far remained within bounds and therefore not yet given rise to serious concern. The deterioration for the Community as a whole, however, is beginning to gather momentum. The Community's balance of trade (cif-fob), which showed a surplus of $1750 million in 1968 and was in equilibrium in 1969, will probably close with a deficit of some $1500 million in 1970. The surplus on current account, which was some $5000 million in 1968 and had declined to some $3500 million in 1969, will probably be down to between $1500 and $2000 million in 1970.

In 1968 and 1969, the level of net foreign exchange reserves held by the monetary authorities and the commercial banks in the Community fluctuated appreciably as a result of speculative movements and the parity changes. Since the spring of 1963, when these reserves touched their highest point in the post-year period, they have fallen by about one third, but nevertheless they still amount to some $18 000 million.

3. *Situation and outlook in the member countries*

These essential features of the economic situation in the Community as a whole are, in varying degree, also to be found in the individual member countries.

In *Germany,* economic activity has continued to expand rapidly. It would appear, however, that the unprecedented degree of capacity utilization no longer leaves room for industrial production to go up as rapidly as last year. Since the revaluation of the mark, the expansion of demand has fed less on exports and more on components of domestic demand such as fixed investment by enterprises and private consumption. The labour market is under heavy strain: in May, the number of unfilled vacancies was eight times that of the number of applicants for jobs. Wage costs have continued to soar: in the first quarter of 1970, actual earnings in trade and industry as a whole were 14% up on a year earlier. The slower rise in the cost of living during the past few months appears to be mainly the result of fortuitous factors. In May, the consumer price index was 2.3% higher than in December 1969. For the first five months of 1970, the trade balance showed a surplus of $1400 million, repeating the performance of a year earlier. The current account, however, has ceased to show more than a small surplus, while the basic balance of payments is in heavy deficit as a result of exports of long-term capital The strains on the German money and capital markets have of late induced banks and firms to borrow in larger measure from abroad. The net reserves of the central bank (including special drawing rights) therefore went up by DM 2200 million during the first five months of 1970.

Although demand has of late been growing more slowly, the current state of order books, the foreseeable expansion of incomes of households, and the scale of investment plans of enterprises suggest that, during the period till the end of the year, economic activity will remain lively and prices will continue to go up.

In *France,* external equilibrium was restored during the early months of 1970. Internal equilibrium, on the other hand, has not yet been fully re-established. While private consumption increased only very modestly in recent months, investment demand was firm and the trend of export demand continued upwards. Industrial production went on expanding at a satisfactory pace. Admittedly, the monthly index of industrial production (excluding construction, and adjusted for seasonal variations) remained stable from February to April, but it does not take account of the trend in activity in most capital goods industries, where expansion continued unabated. On the labour market, unemployment tended to increase a little. The upward thrust of wages and prices has not eased yet. In the first quarter of 1970, hourly wage rates in trade and industry were about 10% higher than a year earlier. Consumer prices rose by 2.7% during the first five months of 1970. The deficit on the trade balance (cif-fob) for the period January-May 1970 was $587 million, as against $1100 million a year earlier. In the first five months of 1970, net receipts of foreign exchange by the monetary authorities totalled $1400 million, owing to an improvement in the pattern of leads and lags, the position on the services account and the inflow of capital from abroad; one result of this was that the short-term debt contracted with foreign central banks could be repaid in full. Budgetary expenditure was handled in a way that had an appreciable contractive influence on domestic liquidity. In the past few months, however, bank lending to business has tended to expand, if only slightly.

In the months ahead, a certain slackening in the expansion of overall demand may well lead to a slowdown in economic growth, but the rise in wages and prices is liable to be more vigorous than one would wish.

In *Italy,* the social tensions of autumn 1969 and their reappearance in 1970 had a heavy impact on economic development. Domestic demand, which had been hit at first by the loss of revenue caused by the strikes, has expanded again, mainly because of substantial wage increases over a comparatively short period. Production has picked up but, owing to the disturbances affecting trade and finance patterns and to the vicissitudes of the social situation, recovery has fallen distinctly short of expectations. As a result, a large part of demand was not met, and this gave rise to sharp disequilibria. In the first quarter of 1970, hourly wage rates in trade and industry as a whole were on average almost 17% higher than a year earlier. The rise in consumer prices gathered distinct momentum, reaching 2.1% from December 1969 to April 1970. The balance of trade for the first five months of 1970 showed a deficit of $739 million whereas it had been in equilibrium during the same period of 1969. Net foreign exchange holdings of the monetary authorities fell by $775 million during the first four months of the year. Treasury transactions again closed with a heavy deficit, financed by major calls on the central bank.

Re-establishment of a better social climate is indispensable if the economic situation in Italy is to be stabilized, from the angle of both production and internal and external equilibrium.

In the months ahead this stabilization will, in addition, depend on the way in which demand will develop in relation to the still substantial scope for an increase in domestic production.

In the *Netherlands,* exports continued to forge ahead as a result of the boom obtaining in the Community, especially in Germany; at the same time there was a lively advance in fixed investment by enterprises and private consumption. Industrial production has risen rapidly in the past few months and the strains on the labour market have become even more acute. In the first quarter of 1970, hourly wage rates were 7% up on the same period of the previous year. Prices are still climbing appreciably: in May, the consumer price index was 2.7% higher than in December 1969. In the first five months of 1970 the trade balance showed a considerably heavier deficit than in the same period of 1969 ($610 million as against $475 million). Between December 1969 and May 1970, net foreign exchange holdings of the central bank increased by $127 million. Bank lending to business and private customers, expanding vigorously again, and the cash operations of the public authorities kept domestic liquidity at a high level.

In all probability, the pressure of demand will remain heavy during the months ahead. The middle of the year will bring major rises in index-linked wages. As fixed investment by enterprises will also go on expanding vigorously, balanced growth will continue to be difficult to achieve.

In *Belgium,* exports have been rising sharply again in the past few months, following a sluggish period at the beginning of the year. The trend in fixed investment by enterprises has been particularly dynamic, and private consumption has continued its brisk advance. There has been an appreciable rise in industrial production. If account is taken of the high percentage of less skilled workers in the total number of job applicants, and of the structure of the manpower reserves in relation to the pattern of unfilled vacancies, the labour market must be considered to be under strain. Consumer prices in the first five months of 1970 went up by 1.7%. The trade surplus ($82 million) in January-April 1970 was distinctly higher than a year earlier. The gross reserves of the central bank fell by more than $30 million during the first six months of the year. The expansion of bank lending to enterprises and the cash operations of the public authorities helped to increase domestic liquidity.

In the light of the foreseeable trend of domestic and export demand, the pressure on prices and costs must be expected to continue in the second half of 1970.

In *Luxembourg,* there have been some signs of an easing of pressures in the business situation in recent months, especially because of a weaker trend on the world market for steel. The growth of industrial production has slowed down. Consumption and investment, however, have expanded at a very lively pace. The price control measures adopted last November have so far helped to curb the rise in the cost of living touched off by the introduction of VAT. From December 1969 to May 1970, the consumer price index went up by 2.8%.

For the months ahead, a vigorous expansion in domestic demand and a persistence of the rise in costs must be expected.

II. Guidelines for the Community's short-term economic policy

The unstable character of the world economic situation, the danger of self-reinforcing inflationary pressures within the Community, the risk of a clear deterioration in the competitive position of Community industries, the social consequences of a persistent rise in consumer prices, are reasons enough for insisting that a moderating economic policy should be maintained in the countries of the Community.

In its Memorandum to the Council of 22 December 1969, the Commission envisaged the possibility of a change in the Community's economic policy during 1970 if it should be necessary to offset a slowdown in economic activity stemming either from international causes or from specific factors in member countries. Under the present circumstances, such a change would not appear to be appropriate.

In all Member States it will still be essential that action aimed at progressively re-establishing the fundamental equilibria in the economy is continued firmly, so that the Community will not—in the more or less short term—have to recover its stability at the expense of a reversal in the economic trend that would affect the level of employment.

The policy of regulating overall demand must be pursued in a way that will reduce excess demand in all the sectors where it persists, so as to check the cost inflation which, in the long run, is a menace to growth; but it must equally aim at preserving the economy from prolonged stagnation or recession. These aims will be achieved by using the various instruments of economic policy simultaneously, in a mix that is appropriate to the circumstances.

1. At the present time, the task of restoring stability is devolving mainly on action to restrain credit. Most Member States are rigorous in taking such action. During the next few months the restrictive line must be maintained everywhere, in view of the prospective trend of production, incomes and prices in the Community, and of the international monetary situation. Even if it should appear necessary to make changes in this policy in certain member countries, they must not compromise its overall effectiveness.

Credit policy seems nevertheless to have reached the limits of its usefulness in several member countries; its effects are also liable to be counteracted by an influx of foreign capital, in the absence of specific measures to meet this influx. It must be strengthened by other instruments.

2. In the next few months budget policy will have a vital contribution to make to the achievement of balanced growth.

Since submitting its Memorandum to the Council in July 1969, the Commission has stressed the need for not letting the whole weight of control of economic trends rest on credit policy alone; the excessive use of this instrument may, in fact, have baneful effects on the growth of the economy. At the same time, the Commission had advocated a more important role for budget policy in the mix of economic policy instruments, in order to implement a more comprehensive and better balanced overall policy against inflation.

In all Member States, the increase in government spending must, in the current economic situation, be contained within narrow limits. The efforts to curb spending should nevertheless affect productive investment by governments and investment in public facilities and infrastructure as little as possible. Measures to increase tax receipts should, where appropriate, not be ruled out as a means of reducing the excessive growth in consumption and private investment. At all events, any extra receipts should be used in a way that helps to reduce internal liquidity.

In Germany, more stringent measures in the field of public finance are all the more desirable because credit policy is already very restrictive. In France, the persistent rise in prices and the growth in production, which is faster than anticipated, justify a strictly balanced budget and, considering the probable increase in tax receipts, even a budget surplus. In Italy, where demand has outstripped production, there is a need for more stringent budget policy both on the expenditure and on the revenue side. The budget deficit should be financed out of savings rather than by direct or indirect recourse to monetary means. The necessary austerity should however be exercised in a way that affects the growth of investment as little as possible, in order not to endanger the outlook for growth over the medium term and the level of employment. In the Netherlands, budget policy, which is still providing unduly strong stimuli, must be modified in such a way as to limit public expenditure more strictly and so reduce the budget deficit. In Belgium, the contingency appropriations in the central government budget should not only remain frozen throughout 1970 but immediate efforts must be made to reduce the deficit on the budget. In Luxembourg, budget policy must in particular serve to reduce excess demand in the building sector, which is a specific source of inflation.

Now that Member States are beginning to prepare their 1971 budgets, financial stringency remains essential, for there is nothing to suggest that between now and the middle of 1971 the inflationary pressures will be completely under control. If budget policy were to be too easygoing, it would entail particularly unfortunate psychological consequences, for it would be likely to prompt or to revive inflationary behaviour by certain transactors. If a more flexible economic policy should become necessary during 1971, it is in the field of credit policy that the relaxation could begin.

3. Under the present economic conditions, where in all Member States the rise in wages and salaries is outstripping productivity gains in disquieting measure, it is particularly desirable that the public authorities and both sides of industry should jointly look for means which will allow the various types of income to evolve in a way more in line with the scope for growth in production and with the need to safeguard general economic equilibrium. If present trends do not change, serious consequences for the standard of living and the level of employment will be unavoidable. In this context, it would be worthwhile to examine ways of incorporating in wages and salaries an element which would give wage and salary earners a share in their firms' profits and would establish a more direct link between investment and saving. As it has already done, some little time ago, the Commission again stresses the advisability of a policy to stimulate saving.

4. Lastly, measures to increase competition, rationalize the production apparatus and distribution channels, and adjust workers' skills to the continuously changing needs of the economy, remain as necessary as ever; they will serve to reduce the still wide gap between production potential and demand while helping to maintain a satisfactory level of employment.

The Commission requests the Council to approve the guidelines set out above and to invite the member States to use them as a model for the economic policies to be applied in the coming months.